No. 91-641

IN THE

Supreme Court of the United States

OCTOBER TERM, 1991

RICHARD A. FENN; JAMAL RADWAN; SAUDI EUROPEAN INVESTMENT CORPORATION N.V.; ALEF INVESTMENT CORPORATION N.V.; ALEF BANK, S.A.,

Petitioners,

—v.—

ABDULAZIZ A. ALFADDA; ABDULLAH ABBAR; ABDULLA KANOO; ABDULAZIZ KANOO; YUSIF BIN AHMED KANOO (a Partnership Company); AHMED A. ZAINY,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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QUESTIONS PRESENTED

1. Does the civil RICO statute apply to foreign investors' overseas purchase of shares in a privately-held foreign company merely because of incidental uses of the United States wires or mails in connection with purchases by other foreign investors not parties to the litigation?

2. Should the "substantial conduct or effects in the United States" test for determining United States subject matter jurisdiction be replaced in the civil RICO context by a test in which two predicate acts involving the wires or mails in the United States suffice to make an otherwise wholly foreign transaction subject to United States substantive law?

PARTIES TO THE PROCEEDING

The parties to this proceeding are:

1. Petitioner Saudi European Investment Corporation N.V.*
2. Petitioner Alef Investment Corporation N.V.**
3. Petitioner Alef Bank, S.A.**
4. Petitioner Richard A. Fenn.
5. Petitioner Jamal Radwan.
6. Defendant Société de Banque Privée, S.A., formerly Saudi European Bank, S.A.***
7. Respondent Abdulaziz A. Alfadda.
8. Respondent Abdullah Abbar.
9. Respondent Abdulla Kanoo.
10. Respondent Abdulaziz Kanoo.
11. Respondent Yusif Bin Ahmed Kanoo, a partnership company.
12. Respondent Ahmed A. Zainy.

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* Saudi European Investment Corporation N.V. is a privately-held Netherlands Antilles corporation. The following are or may be considered subsidiary companies of Saudi European Investment Corporation N.V.: Saudi Arabian and European Finanz Corporation B.V. and SER Colombes.

** Alef Investment Corporation N.V. is a privately-held Netherlands Antilles corporation and is the corporate parent of Alef Bank, S.A., a French bank.

*** Société de Banque Privée, S.A. is not a party to this petition.

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

Saudi European Investment Corporation N.V. ("SEIC"), Alef Investment Corporation N.V., Alef Bank, S.A., Richard A. Fenn and Jamal Radwan respectfully petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the Second Circuit, entered in this case on June 5, 1991, which reversed the decision of the United States District Court for the Southern District of New York dismissing the amended complaint for lack of federal subject matter jurisdiction.

OPINIONS BELOW

The opinion of the court of appeals is reported at 935 F.2d 475 (2d Cir. 1991). The opinion of the district court dismissing the amended complaint is reported at 751 F. Supp. 1114 (S.D.N.Y. 1990). These opinions are reprinted in the Appendix to this Petition.[1]

JURISDICTION

The judgment of the court of appeals reversing the judgment of the district court was entered on June 5, 1991. A timely petition for rehearing and a suggestion for rehearing *en banc* was denied on July 16, 1991. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATUTES AND RULES INVOLVED

The statute involved in this proceeding is Title IX of the Organized Crime Control Act of 1970, 18 U.S.C. § 1961 *et seq.* (commonly known as "RICO"), a copy of which is reprinted in the Appendix.

STATEMENT OF THE CASE

This is a case brought by six Middle Eastern investors arising out of their 1984 purchase of shares in SEIC, a privately-held foreign corporation. The shares were bought and paid for abroad, and the purchasers concede that any representations concerning the transaction were made to them abroad. In these circumstances, the Second Circuit Court of Appeals nevertheless found United States subject matter jurisdiction under the civil RICO statute. The court of appeals thus necessarily found that the substantive law applicable to these wholly foreign transactions is United States law.

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1 References to "_____ a" are to pages of the Appendix.

The Second Circuit fell into this error by departing from the test of "substantial conduct or effects in the United States" that has been widely employed to limit the application of United States statutes to international transactions, instead taking the view that two predicate acts involving the United States mails or wires suffice to establish civil RICO jurisdiction. Given the central role of United States communications systems in international commerce, the consequence of the Second Circuit's ruling is to make almost any alleged fraud in international business subject to the RICO statute and the jurisdiction of the United States courts. As the district court had warned in dismissing the amended complaint, "[g]iven the vast number of foreign and transnational business transactions in which United States mails, wire and telephone systems are used merely by happenstance, United States courts could become flooded with countless foreign based RICO claims bearing little or no nexus to this country." (26a.)

The Second Circuit's view of civil RICO's jurisdictional reach is unsupported by RICO's statutory language or legislative history, and squarely conflicts with the *en banc* decision of the Ninth Circuit in *Republic of the Philippines v. Marcos*, 862 F.2d 1355, 1358-59 (9th Cir. 1988), *cert. denied*, 490 U.S. 1035 (1989), and every other reported decision, all of which require either substantial conduct by defendants in the United States or significant adverse effects in the United States as a result of defendants' actions before accepting jurisdiction over RICO claims.[2]

The Parties

Petitioner SEIC is a closely-held Netherlands Antilles corporation which formerly owned defendant Saudi European

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2 *See Philan Ins. Ltd. v. Frank B. Hall & Co.*, 748 F. Supp. 190, 193-95 (S.D.N.Y. 1990) (court lacked subject matter jurisdiction over RICO claims where there was neither substantial conduct nor substantial effects in the United States); *United States v. Noriega*, 746 F. Supp. 1506, 1517 (S.D. Fla. 1990) (stating that "[a]s long as the racketeering activities produce effects or are intended to produce effects in this country, RICO applies").

Bank, S.A., a French bank now known as Société de Banque Privée, S.A. Petitioner Alef Investment Corporation N.V. is the Netherlands Antilles parent of petitioner Alef Bank, S.A., a French bank with its principal offices in Paris. Petitioner Jamal Radwan is managing director of SEIC and resides in Europe. Petitioner Richard A. Fenn, a New York resident, is a former officer of SEIC and former director of Saudi European Bank, S.A.

Respondents Abdulaziz A. Alfadda ("Alfadda"), Abdullah Abbar ("Abbar"), Ahmed A. Zainy ("Zainy"), Abdulla Kanoo, Abdulaziz Kanoo and Yusif Bin Ahmed Kanoo ("the Kanoos") are foreign residents and nationals of Saudi Arabia or Bahrain. Respondents claim that in 1984 they were misled into investing in SEIC on the basis of a private placement memorandum and oral representations delivered entirely abroad. They brought this action in September 1989 alleging a RICO claim, federal securities fraud[3] and common law claims based upon their 1984 SEIC share purchases.

The 1984 Private Placement

In mid-1983, SEIC decided to make a private placement of its shares to selected investors located in the Middle East and Europe. (E 637.)[4] To assist in its private placement, SEIC prepared a confidential private placement memorandum (the "Private Placement Memorandum") in Paris. (A 170-83.) The Private Placement Memorandum expressly stated that shares in the private placement would not be sold to residents or nationals of the United States. (A 171.) No United States resident or entity purchased SEIC shares in the private placement. (E 640.)

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3 Since respondents' securities claims are time-barred under this Court's recent decision in *Lampf, Pleva, Lipkind, Prupis & Petigrow v. Gilbertson*, 111 S. Ct. 2773 (1991), this Petition is limited to the issue of RICO subject matter jurisdiction.

4 References to "A _____" and "E _____" are to the pages of the Joint Appendix and Exhibits, respectively, filed in the court of appeals. The record has not been certified to the Court at this time, but will be done so upon the Court's request.

Respondents concede that they are neither United States residents nor nationals. (A 123.) Respondents who claim to have purchased SEIC shares in the 1984 private placement—Abbar, Zainy and the Kanoos—do not dispute that the Private Placement Memorandum was sent to them, if at all, from Paris or Geneva or hand-delivered in Saudi Arabia and Bahrain. (18a; E 639, 641.) Respondents' counsel also conceded that any oral representations to his clients regarding the SEIC offering were made entirely in the Middle East or Europe. (A 107: "[N]one of these plaintiffs had the representations made to them, physically made to them, in the United States. We don't dispute that.") Finally, the undisputed proof showed that all respondents purchased their SEIC shares outside the United States.[5]

This Litigation

On June 20, 1990, following discovery limited to subject matter jurisdiction, respondents filed an amended complaint. (A 121-84.)[6] As noted by the district court, "the amended complaint alleges facts claimed to be relevant to subject matter jurisdiction in great detail." (28a.) Defendants then moved on the extensive evidentiary record to dismiss the

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5 Abbar and Zainy gave instructions from Saudi Arabia to their banks in Saudi Arabia and Switzerland to make payments to SEIC's account in Paris; payment was subsequently made to SEIC's account in Paris, and Abbar and Zainy's accounts were debited in Saudi Arabia and Switzerland. The Kanoos paid for their shares by instructing the London branch of their Saudi Arabian bank to make payment to SEIC's account at the Bahrain branch of Saudi European Bank, S.A.; SEIC's account was credited in Bahrain and the Kanoos' account was debited in London. (E 496-97, 640-41, 697-729.) Alfadda, who alleged that he purchased shares of SEIC in 1979, does not claim to have purchased those shares in the United States. (A 129.)

6 Respondents filed their original complaint in this action on September 20, 1989. Although petitioners moved to dismiss the complaint on its face on grounds of lack of subject matter jurisdiction and *forum non conveniens* (A 2), the district court permitted respondents to conduct discovery concerning petitioners' alleged activities in the United States in order to ensure that the factual bases for subject matter jurisdiction were fully explored. (14a; A 73.) Neither the district court nor the court of appeals determined the issue of *forum non conveniens*.

amended complaint for lack of subject matter jurisdiction. (A 4.)

The District Court's Decision

On November 27, 1990, the district court dismissed the amended complaint for lack of subject matter jurisdiction. (12a-28a.) Noting its authority to resolve factual disputes in an evidentiary attack upon respondents' jurisdictional allegations (19a),[7] the district court made the following factual findings:

- Respondents are all foreign nationals residing outside the United States (13a, 20a, 24a-25a);
- Five of the six petitioners are foreign entities or foreign residents (24a-25a);
- SEIC is a closely-held foreign corporation, and its stock has never been traded on any United States exchange (14a, 19a);
- The Private Placement Memorandum upon which respondents allegedly relied "cannot be said to have emanated from" the United States (19a);
- The Private Placement Memorandum "was sent to the plaintiffs from Paris or Geneva, or hand delivered in Saudi Arabia or Bahrain" (18a);
- Any communication of allegedly fraudulent representations to respondents took place outside the United States (24a);
- Any effects of petitioners' activities were felt by foreign nationals outside the United States (24a); and
- Petitioners' actions in the United States were at most "subsidiary" to the fraud alleged by respondents. (25a.)

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7 *See Thornhill Publishing Co. v. General Tel. & Elec. Corp.*, 594 F.2d 730, 733 (9th Cir. 1979) (and cases cited therein); *Exchange Nat'l Bank v. Touche Ross & Co.*, 544 F.2d 1126, 1130-31 (2d Cir. 1976); 13 C. Wright, A. Miller & E. Cooper, *Federal Practice & Procedure: Jurisdiction 2d* § 3522, at 63-65 (1984).

The district court then analyzed these facts within the framework of the "conduct" test for determining whether United States or foreign law should govern securities transactions. (16a-21a.)[8] The district court observed that respondents had failed to show that "substantial conduct directly causing injuries" to them had taken place in the United States. (16a-20a.) The district court concluded that, where respondents were foreign nationals alleging reliance on a misleading prospectus which they had received abroad, the place of the alleged fraud was outside of the United States. (19a-20a.) The district court also concluded that respondents, who suffered any alleged injury abroad, had failed to satisfy the "effects" test for extraterritorial application of the federal securities laws, since they did not establish substantial effects in the United States upon which they could rely. (20a.)[9]

The district court then analyzed respondents' assertion of subject matter jurisdiction over their RICO claim, which is based on the same allegations as the federal securities fraud claim, in light of the limitations upon extraterritorial application of United States law set forth in the "conduct" and "effects" tests described in the cases and the *Restatement (Third) of the Foreign Relations Law of the United States* (1987). (21a-27a.) Relying on its factual findings that the great bulk of petitioners' alleged conduct took place outside the United States and the alleged damages occurred to foreign nationals outside the United States, the district court dismissed respondents' RICO claim despite the alleged existence of subsidiary "predicate acts" in the United States:

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8 *See, e.g., Bersch v. Drexel Firestone, Inc.*, 519 F.2d 974, 987 (2d Cir.) ("[W]e see no reason to extend [jurisdiction] to cases where the United States activities are merely preparatory or take the form of culpable nonfeasance and are relatively small in comparison to those abroad"), *cert. denied sub nom. Bersch v. Arthur Andersen & Co.*, 423 U.S. 1018 (1975).

9 *See, e.g., Consolidated Gold Fields PLC v. Minorco, S.A.*, 871 F.2d 252, 261-62 (2d Cir.) ("In determining whether certain effects qualify as 'substantial,' courts have been reluctant to apply our laws to transactions that have only remote and indirect effects in the United States . . ."), *cert. dismissed*, 492 U.S. 939 (1989).

> "The structure of RICO is such that it will no doubt often be possible to include in a RICO complaint challenging a transnational transaction some subsidiary predicate acts taking place in the United States. Where, however, as here and in so many RICO cases, the heart of the claim is fraud in the sale of securities, there is no basis for thinking that Congress intended predicate acts which are either preparatory, or constitute the after-the-event working out of an already completed fraud, to confer otherwise non-existent subject matter jurisdiction.
>
> "Therefore, the Court holds that *when the RICO predicate acts occurring in the United States consist of subsidiary uses of United States communications and transportation systems, but the underlying fraud occurs outside the United States, the Court lacks subject matter jurisdiction over the RICO claim. The tail should not wag the dog.*"

(25a) (emphasis added). In so doing, the district court expressly rejected respondents' attempt to rely on the alleged incidental use of United States wires or mails in connection with purchases by other foreign investors not parties to this litigation. (*Id.*)

The Second Circuit's Decision

The court of appeals did not disturb a single factual finding made by the district court. It did not dispute that respondents purchased their shares of SEIC in 1984 in the Middle East, or that any representations to respondents regarding those share purchases were made in the Middle East or Europe. The Second Circuit nevertheless reversed the district court's dismissal of respondents' RICO and securities law claims, announcing a new rule for the exercise of subject matter jurisdiction over civil RICO allegations.

The court of appeals began by finding jurisdiction over respondents' securities law claim based upon allegations of peripheral use of United States mails and wires in relation to subsequent purchases of SEIC shares by nonparties

Abdulrahman Al-Turki ("Al-Turki"), a foreign national and Saudi Arabian resident, and Lincoln American Investment Company N.V. ("Lincoln N.V."), a Netherlands Antilles subsidiary of a United States corporation formed for the specific purpose of creating an offshore entity eligible to purchase in the SEIC share offering. (5a-9a.)[10]

The court of appeals then addressed the jurisdictional reach of RICO. (9a-11a.) The court first noted that the statutory language of RICO is silent as to its extraterritorial application, and recognized a "dearth" of precedent in the Second Circuit on that question. (9a.) After observing that RICO may reach foreign entities operating in the United States, the court of appeals grounded subject matter jurisdiction over respondents' RICO claim entirely upon the alleged occurrence "primarily in the United States" of peripheral acts—here, the incidental alleged use of United States mails and wires in the subsequent purchases of SEIC shares by nonparties Al-Turki and Lincoln N.V. (10a-11a.)[11]

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10 The court of appeals sought to bolster its reliance on wire and mail usage in the United States by reference to allegations that petitioners "completed" the alleged fraud by diluting respondents' SEIC shareholdings through the Al-Turki and Lincoln N.V. sales. (8a.) This is curious, since any fraud upon respondents would have been complete as soon as respondents paid for their shares, and because the record is uncontradicted that SEIC did not oversell its offering of 600,000 shares: no more than 600,000 shares were sold in the private placement, and the purchase by Al-Turki occurred well after the offering closed. (E 734-35, 765, 775-778.) Even respondents do not claim that Lincoln N.V.'s purchase itself resulted in the sale of over 600,000 shares. (A 142-45.)

11 The Second Circuit relied on respondents' allegations of one telephone conversation between Jamal Radwan in Paris and Al-Turki, travelling in Houston, and three telexes between Al-Turki and SEIC in Paris shortly thereafter. (6a, 8a.) The proof showed that Al-Turki, a Saudi Arabian, negotiated his purchase of SEIC shares abroad, and the incidental communications Al-Turki received during his trip to Houston took place weeks after the date by which he had finally decided to purchase those shares. (E 734, 765, 882.) The alleged use of

REASONS FOR GRANTING THE WRIT

This petition should be granted because the Second Circuit's decision has thrown open the gates to a flood of civil RICO lawsuits brought by foreign plaintiffs attacking foreign transactions in foreign securities or foreign goods,[12] with drastic implications for United States courts and the relationships of the United States with other countries which understandably assume that their own laws will apply to transactions occurring within their borders.[13] As the district court correctly recognized when it dismissed respondents' RICO claim despite the alleged existence of subsidiary predicate acts in the United States, a result finding jurisdiction would be disastrous:

> "If the Court were to hold otherwise, then jurisdiction would be sustained over a foreign plaintiff's RICO claim solely because the RICO defendants made, say, two telephone calls within the United States, or used the United

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U.S. wires and mails relied on by the court of appeals in the Lincoln N.V. transaction—one letter and one telex—focussed on the formation of that offshore entity in order to comply with SEIC's prohibition on the sale of its shares to U.S. entities. (5a, 8a-9a; E 68, 71, 628-29, 642-43.)

12 The Second Circuit's opinion has received widespread attention in the financial and legal press: *RICO Applies To Securities Fraud Cases Involving Trades Abroad, Court Rules*, Wall St. J., June 7, 1991, at B4, col. 3; *Saudi Investors' Right to Sue in Fraud Case Upheld*, L.A. Times, June 7, 1991, at D5, col. 2; *Appeals Court Allows RICO Case Filed by Saudi Nationals*, Reuters Bus. Rep., June 6, 1991; *Foreign Investors Win Appeal to Bring Fraud Claims in the U.S.*, N.Y.L.J., June 7, 1991, at A1, col. 1; *Corporate Update*, N.Y.L.J., June 20, 1991, at 5; *Foreign Investors May Proceed with Securities, RICO Claims, CA 2 Finds*, 23 Sec. Reg. & L. Rep. (BNA) No. 24, at 903 (June 14, 1991); *New Court Decisions: Racketeering: Jurisdiction*, 59 U.S.L.W. 2767 (June 25, 1991).

13 Before filing suit here, respondents instituted proceedings in the Netherlands Antilles attacking under Netherlands Antilles law the same transactions involved here. The Netherlands Antilles suit remains pending. (E 575-625, 678-96.)

> States mails on two occasions. Given the vast number of foreign and transnational business transactions in which United States mails, wire and telephone systems are used merely by happenstance, United States courts could become flooded with countless foreign based RICO claims bearing little or no nexus to this country. While it is no doubt true that implementation of RICO has exceeded Congress' original vision of the statute (*see generally*, Lynch, *RICO: The Crime Of Being A Criminal*, 87 Colum. L. Rev. 661, 920 (1987)), plaintiffs have cited nothing in either the statutory language or its legislative history to indicate that Congress would consider it desirable to apply RICO to expand the jurisdiction of the federal courts so prodigiously."

(26a-27a.)

The extreme notion that United States law should be extended to apply to foreign purchases by foreigners of stock in a foreign corporation directly conflicts with the traditional limitations developed by the federal courts and embodied in the *Restatement (Third) of the Foreign Relations Law of the United States* for the extraterritorial application of federal law. Those limitations correctly apply to the extraterritorial reach of civil RICO.

The Second Circuit's contrary statement in its penultimate sentence—grounding RICO subject matter jurisdiction upon the alleged occurrence of peripheral acts in the United States—cannot be the law. If it were, even such routine acts as consultation with American counsel or routing funds through United States banks could be deemed "predicate acts" sufficient to invoke RICO subject matter jurisdiction over overwhelmingly foreign transactions.

THE SECOND CIRCUIT'S HOLDING THAT THE ALLEGED OCCURRENCE IN THE UNITED STATES OF PERIPHERAL PREDICATE ACTS IS SUFFICIENT TO CREATE RICO SUBJECT MATTER JURISDICTION IS DANGEROUS AND UNSUPPORTABLE.

A. The Second Circuit Departed From Traditional Limitations On The Extraterritorial Application Of Domestic Law.

The jurisdictional test for civil RICO established by the court of appeals in this case begins and ends with a single inquiry: whether there is jurisdiction in the United States to prosecute any two "predicate acts" alleged by a RICO plaintiff. As the district court in this action recognized, that test is unsupported by RICO's statutory language or its legislative history, unsupported by precedent, and disastrous as policy.

Subject to the constraints of due process and Article III of the Constitution, it is for Congress to decide the degree to which legislation should apply to transactions with extraterritorial dimensions. *Finley v. United States*, 490 U.S. 545, 548 (1989); *Insurance Corp. of Ireland, Ltd. v. Compagnie des Bauxites de Guinee*, 456 U.S. 694, 701 (1982); *Zoelsch v. Arthur Anderson & Co.*, 824 F.2d 27, 29 (D.C. Cir. 1987); *Leasco Data Processing Equipment Corp. v. Maxwell*, 468 F.2d 1326, 1334 (2d Cir. 1972); C. Wright, *The Law of Federal Courts* § 10, at 37 (4th ed. 1983); *see generally* Brilmayer, *The Extraterritorial Application of American Law: A Methodological & Constitutional Appraisal*, 50 Law & Contemp. Probs. 11, 16 (Summer 1987).

The RICO statute, however, is silent as to its extraterritorial application. (9a, 33a-52a.) The extensive legislative history of RICO also contains no expression of Congressional intent to reach transactions abroad. H.R. Rep. No. 1549, 91st Cong., 2d Sess., *reprinted in* 1970 U.S. Code Cong. & Admin. News 4007, 4010, 4032-4036; S. Rep. No. 617, 91st Cong., 1st Sess. 76-83, 121-128, 157-214 (1969). There is thus no basis for believing that Congress intended RICO to reach

transactions by foreigners that occur primarily outside the United States and which have no substantial effects in the United States.

This Court has held that, absent indications of contrary intent, legislation should be presumed to apply only domestically. *Foley Brothers v. Filardo*, 336 U.S. 281, 285 (1949); *see Zoelsch v. Arthur Anderson & Co.*, 824 F.2d 27, 31 (D.C. Cir. 1987). However, in a world marked by technological development and increase of cross-border transactions, the lower courts have taken a more expansive view of statutory reach where no specific Congressional intent has been expressed.

In recent times, where Congress has been silent, the courts of appeals uniformly have applied a test of substantial conduct or effects in the United States to determine whether a transnational transaction is to be governed by United States law. The *Restatement (Third) of Foreign Relations Law of the United States* has adopted this test as a general test of subject matter jurisdiction. In every RICO case decided prior to this one, courts have applied the same test.

Thus, faced with the issue of jurisdictional reach of the Securities Exchange Act of 1934, 15 U.S.C. § 77b *et seq.* (1988), and the Commodity Exchange Act, 7 U.S.C. § 1 *et seq.* (1988)—also silent as to their extraterritorial application—the federal courts of appeals have unanimously determined that securities or commodities fraud claims must be dismissed for lack of subject matter jurisdiction where a plaintiff cannot show either substantial United States "conduct" in connection with the sale of securities or commodities or significant adverse "effects" in the United States arising from that sale.[14] These tests appropriately apply to the determination of RICO subject matter jurisdiction.

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14 *See, e.g., Consolidated Gold Fields PLC v. Minorco, S.A.*, 871 F.2d 252, 261-62 (2d Cir.), *cert. dismissed*, 492 U.S. 939 (1989); *Zoelsch v. Arthur Andersen & Co.*, 824 F.2d 27, 33 (D.C. Cir. 1987); *Tamari v. Bache & Co. (Lebanon) S.A.L.*, 730 F.2d 1103, 1107 (7th Cir.), *cert. denied*, 469 U.S. 871 (1984); *Grunenthal GmbH v. Hotz*, 712 F.2d 421,

The *Restatement (Third) of the Foreign Relations Law of the United States* sets forth the "conduct" and "effects" tests as general limitations upon the exercise of subject matter jurisdiction by a sovereign state. *Restatement* §§ 402, 403 (state may only exercise jurisdiction over conduct which occurs "wholly or in substantial part" within its territory or has a "substantial effect" within its territory, and even then only where reasonable to do so). Similarly, considerations of international comity counsel restrictions on the extraterritoral application of domestic law. *See id.* § 403(1) and comment a; *Consolidated Gold Fields PLC v. Minorco, S.A.*, 871 F.2d 252, 263 (2d Cir.), *cert. dismissed*, 492 U.S. 939 (1989); *see generally* Note, *Predictability and Comity: Toward Common Principles of Extraterritorial Jurisdiction*, 98 Harv. L. Rev. 1310 (1985).

It is thus impossible fairly to construe RICO to apply to an alleged "pattern of racketeering activity"[15] in which the great bulk of the alleged conduct forming the pattern (*i.e.*, the alleged fraudulent scheme) occurred overseas, the United States conduct was incidental at most, and there were no effects or continuing threat of criminal activity in the United States.

No other federal court has endorsed the basis for RICO subject matter jurisdiction established by the court of appeals in this case. In *Republic of the Philippines v. Marcos*, 862 F.2d 1355 (9th Cir. 1988) (en banc), *cert. denied*, 490 U.S. 1035 (1989), the Ninth Circuit addressed RICO claims against

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424-25 (9th Cir. 1983); *Continental Grain (Australia) Pty. Ltd. v. Pacific Oilseeds, Inc.*, 592 F.2d 409, 417 (8th Cir. 1979); *Securities & Exchange Comm'n v. Kasser*, 548 F.2d 109, 114-15 (3d Cir.), *cert. denied sub nom. Churchill Forest Indus. (Manitoba), Ltd. v. Securities & Exchange Comm'n*, 431 U.S. 938 (1977).

15 This Court has repeatedly noted the importance of RICO's requirement of proof of a "pattern of racketeering activity," set forth in 18 U.S.C. § 1962 (1988). *See H.J. Inc. v. Northwestern Bell Tel. Co.*, 492 U.S. 229, 240-241 (1989); *Agency Holding Corp. v. Malley-Duff & Assocs., Inc.*, 483 U.S. 143, 154 (1987); *Sedima S.P.R.L. v. Imrex Co.*, 473 U.S. 479, 496 n.14 (1985).

the former president of the Philippines and his wife for the conversion and alleged investment in the United States of funds belonging to the Philippine people. Although the *Marcos* court concluded that plaintiff's allegations there were sufficient to establish federal jurisdiction, that determination was based not on the mere commission of some predicate acts within the jurisdiction of the court, but on the occurrence within the United States of sufficient activity to constitute a RICO "pattern". *Id.* at 1358-59. In determining that the pattern of activity in *Marcos* "consisted of operations taking place within the United States . . . [and] had multiple effects on the domestic and foreign commerce of this country," the Ninth Circuit found that the conduct and effects tests for subject matter jurisdiction had been satisfied. *Id.*[16]

No such situation exists here. Respondents, all foreign nationals, claim injury as a result of their entirely foreign purchases of stock in a foreign corporation. The undisputed factual findings of the district court establish that petitioners' conduct took place primarily outside the United States and that any effects on these respondents occurred entirely abroad. Accordingly, the district court properly applied the "conduct" and "effects" limitations to dismiss respondents' alleged RICO claim for lack of subject matter jurisdiction.

B. The Court Should Grant The Writ In Order To Prevent The Disastrous Results Of The Second Circuit's Test For RICO Jurisdiction.

Under the test for RICO subject matter jurisdiction employed by the Second Circuit, even the most peripheral use of domestic banks, wires or mails in connection with a foreign transaction may subject that transaction to RICO claims

16 Similarly, the court in *Philan Ins. Ltd. v. Frank B. Hall & Co.*, 748 F. Supp. 190 (S.D.N.Y. 1990), explicitly imported the "conduct" and "effects" tests to the RICO context in concluding that it lacked subject matter jurisdiction over plaintiff's RICO claims. *Id.* at 193-95. The "effects" test was applied in *United States v. Noriega*, 746 F. Supp. 1506 (S.D. Fla. 1990), to determine that court's exercise of jurisdiction over RICO claims against the former ruler of Panama. *Id.* at 1516-17.

in United States courts.[17] It is not difficult to foresee, as the district court did, that one effect of the Second Circuit's ruling will be that "United States courts could become flooded with countless foreign based RICO claims bearing little or no nexus to this country." (26a.) Foreign business entities may also well shun even the most minimal uses of United States banking facilities or counsel so as not to risk United States litigation over the conduct of their foreign business operations.

The Second Circuit's ruling in this case revived the RICO claim of six Saudi Arabian and Bahraini investors concerning the sale to them in the Middle East and Europe, by means of a private placement memorandum and representations allegedly delivered to them in the Middle East and Europe, of stock in a Netherlands Antilles company. Can RICO lawsuits over purchases by Czech investors of Persian rugs in a Turkish bazaar—confirmed by two telephone calls to New York—be far behind?

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17 Certainly, the holding of the court of appeals in this case has been so understood:

> "The Second Circuit held that although the RICO statute is silent as to its extraterritorial application, where *some* of the predicate acts alleged to show a pattern of racketeering activity occur in the United States, the court has subject matter jurisdiction over the RICO claims."

Bank of Crete, S.A. v. Koskatos, No. 88 Civ. 8412 (KMW) (S.D.N.Y. Aug. 30, 1991) (citing *Alfadda v. Fenn*, 935 F.2d 475, 479 (2d Cir. 1991)) (emphasis added).

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be granted.

Dated: New York, New York
October 15, 1991

Respectfully submitted,

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APPENDIX

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Opinion of the Second Circuit

UNITED STATES COURT OF APPEALS

FOR THE SECOND CIRCUIT

No. 1291—August Term 1990

Argued: April 18, 1991 Decided: June 5, 1991

Docket No. 90-9129

ABDULAZIZ A. ALFADDA, ABDULLAH ABBAR, ABDULLA KANOO, ABDULAZIZ KANOO, YUSIF BIN AHMED KANOO (a partnership company), and AHMED A. ZAINY,

Plaintiffs-Appellants,

—against—

RICHARD A. FENN, JAMAL RADWAN, SAUDI EUROPEAN INVESTMENT CORPORATION N.V., SAUDI EUROPEAN BANK, S.A., ALEF INVESTMENT CORPORATION N.V., and ALEF BANK, S.A.,

Defendants-Appellees.

Before:

LUMBARD, FEINBERG, and MCLAUGHLIN,
Circuit Judges.

Appeal from an order of the Southern District of New York, McKenna, *Judge*, dismissing amended complaint

for lack of subject matter jurisdiction on finding that the transactions complained of transpired overseas.

Reversed and remanded for further proceedings.

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JOSEPH F. HAGGERTY, New York, N.Y. (Shearman & Sterling, New York, N.Y., Danforth Newcomb, Peter L. Lindseth, of counsel), *for Defendant-Appellee Societe de Banque Privee, S.A., formerly Saudi European Bank, S.A.*

LUMBARD, *Circuit Judge*:

Plaintiffs appeal from the November 26, 1990 order of the Southern District of New York, Lawrence M. McKenna, *Judge*, dismissing their amended complaint for lack of subject matter jurisdiction. Plaintiffs, investors in defendant, Saudi European Investment Corporation N.V. (SEIC) allege that they were defrauded[1] when their stake in SEIC was diluted by sales in contravention of an offering prospectus, and that defendants diverted the proceeds from the sales for their personal benefit and the benefit of certain favored SEIC shareholders. The district court held that it had no jurisdiction as it found that the alleged fraud was perpetrated outside the United States. We reverse and remand for further proceedings because of plaintiffs' largely uncontested allegations that fraudulent conduct occurred in the United States.

Plaintiffs, Abdulaziz Alfadda, Abdullah Abbar, Ahmed Zainy, and Abdulla Kanoo, Abdulaziz Kanoo and Yusif Bin Ahmed Kanoo (the latter three plaintiffs referred to as "the Kanoos"), all residents and nationals of Saudi Arabia or Bahrain, filed their complaint in September 1989 naming SEIC, a closely held Netherlands Antilles company[2]; Saudi European Bank, S.A. and Alef Bank, S.A., both French banks; Alef Investment Corporation N.V., a Netherlands Antilles corporation; Jamal Radwan, chair-

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1 The Amended Complaint sets forth causes of action for violations of the Racketeer Influenced and Corrupt Organizations Act, 15 U.S.C. § 1962(a)-(d) (1988), violations of § 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b) (1988), and Rule 10b-5 of the Securities and Exchange Commission, 17 C.F.R. § 240.10b-5 (1990) (plaintiff Alfadda does not join in this count), common law fraud, breach of fiduciary duty and recision of contract.

2 SEIC operated as a holding and/or controlling company of the other corporate defendants.

man of SEIC, and Richard Fenn, former vice-chairman of SEIC, both United States citizens, as defendants.

The Amended Complaint alleges that on or about February 4, 1979, Radwan invited Alfadda to become a shareholder in a proposed company, SEIC. The original stock offering consisted of 20,000 shares at a price of $1,000 per share.[3] In July 1979, Alfadda purchased 1,000 shares of SEIC for $1,000,000. Pursuant to the terms of the 1979 offering, Alfadda and the other holders of the original 20,000 shares distributed were to be given a preference in the offering of new shares, in proportion to the number of original shares held by them.

Around October 1983, Radwan and Fenn planned a second offering of SEIC stock. The original shares were to be subject to a thirty to one split, creating 600,000 shares. The prospectus for the second offering stated that another 600,000 shares (which represented the 20,000 shares which were not issued in the original offering split thirty to one) were to be sold at $100 per share. In the event of an oversubscription, up to 1,800,000 non-voting shares were to be issued. The Kanoos purchased 10,000 shares of SEIC for $1,000,000 on April 9, 1984. On April 2 and 10, 1984, Zainy and Abbar each paid $1,000,000 for 10,000 shares of SEIC.

Plaintiffs allege that despite representations made in the 1984 offering prospectus upon which they relied, 1,200,000 voting shares were sold, thereby diluting their voting interests in SEIC. In addition, Alfadda claims that, despite his reliance upon the representations made to him when he purchased the shares in the original 1979 offer-

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3 Although SEIC had authorized 40,000 shares of its stock, only 20,000 shares were distributed in the 1979 offering.

ing, defendants never informed him of the second offering, thus depriving him of his preferential right to purchase new shares.

Plaintiffs contend, and the defendants do not dispute,[4] that sales to a subsidiary of American Continental Corp. and Abdulrahman Al-Turki, which resulted in the alleged dilution of plaintiffs' voting interests, occurred almost entirely in the United States. In his deposition, Fenn admitted to meeting Charles Keating, chairman of Phoenix-based American Continental, in New York City where Keating informed Fenn that "he would like to take a stake in [SEIC's] capital offering." On May 2, American Continental notified SEIC that its savings and loan subsidiary, Lincoln Savings and Loan Association, wanted to purchase 15% of SEIC's voting shares. Six days after the offer, SEIC telexed American Continental in Phoenix directing it to deposit payment for the shares in a New York bank account. Toward the end of May 1984, Fenn, Radwan and Ronald Reilly, president of Capital International, Inc.,[5] met with Keating and other representatives of American Continental in Phoenix. Although it is not known what was discussed at the meeting,[6] approximately one week later, Fenn telexed Reilly that the $18,000,000 "from American Continental has finally arrived." Because the prospectus had stated that the shares of SEIC would "not be offered or sold directly or indirectly in the United States," American Continental created

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4 Although the defendants disputed the legal significance of the events transpiring in the United States during argument before us, they did not contest their occurrence.

5 Capital International was hired by SEIC to market its private offering.

6 Fenn averred that while the meeting concerned topics unrelated to the SEIC offering, he did not remember what those topics were.

a subsidiary off-shore shell company, Lincoln American Investments N.V., to purchase the SEIC shares.

Plaintiffs also allege that on or around June 20, 1984, Radwan telephoned Al-Turki in Houston[7] to advise him that American Continental agreed to purchase 15% of SEIC's outstanding stock and that if Al-Turki agreed to a large subscription, he, along with Radwan, Keating and another original SEIC investor would control SEIC. On June 22, Reilly telexed Al-Turki to inquire if SEIC could expect an "agreement" on the SEIC offering. Al-Turki sent a return telex to Reilly in which he accepted SEIC's offer to purchase 150,000 voting shares for $15,000,000. On June 26, SEIC telexed Al-Turki in Houston accepting his offer and directing him to deposit his payment in a New York bank account.[8]

In dismissing plaintiffs' securities law claims for lack of subject matter jurisdiction, the district court held that "the fraud was perpetrated by placing the misleading prospectus into the plaintiffs' hands outside the United States." 751 F. Supp. 1114, 1118 (S.D.N.Y. 1990). Apparently considering plaintiffs' allegations of SEIC stock sales to Lincoln American Investments and Al-Turki as irrelevant to the question of jurisdiction, the district court did not consider the import of this alleged conduct in the United States. Accepting plaintiffs' largely uncontested allegations of conduct consummating the fraud in

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7 Al-Turki, a foreign national and resident of Saudi Arabia, owned a Saudi enterprise with offices in Houston.

8 Both Al-Turki and Lincoln's successor in interest, the Resolution Trust Corp., have filed separate lawsuits against these defendants in the Southern District making allegations similar to those in the present case. In the Resolution Trust lawsuit, Townley & Updike, Gadsby & Hannah, Ronald Reilly and Mario Diaz-Cruz III were named as defendants in addition to the defendants in this case.

the United States as true, *see* Wright and Miller, Federal Practice and Procedure § 1350 at 220 (2d ed. 1990) (uncontroverted factual allegations in the body of the complaint taken as true on disposition of motion to dismiss for lack of subject matter jurisdiction), we reverse and remand for further proceedings.

The Securities Exchange Act is silent as to its extraterritorial application. *Cf.* 15 U.S.C. § 78aa (1988) (vesting federal district courts with exclusive original jurisdiction for violations of the Act). Thus, in addressing transnational frauds, courts must ascertain "whether Congress would have wished the precious resources of the United States courts" to be devoted to such transactions. *Psimenos v. E.F. Hutton & Co.*, 722 F.2d 1041, 1045 (2d Cir. 1983) (quoting *Bersch v. Drexel Firestone, Inc.*, 519 F.2d 974, 985 (2d Cir.), *cert. denied*, 423 U.S. 1018 (1975)). Under our decisions, two tests have emerged for determining whether a federal court has subject matter jurisdiction over a foreign plaintiff's claim under the antifraud provisions of the securities laws. Under the "conduct" test, a federal court has subject matter jurisdiction if the defendant's conduct in the United States was more than merely preparatory to the fraud, and particular acts or culpable failures to act within the United States directly caused losses to foreign investors abroad. *See Psimenos*, 722 F.2d at 1046 (citing *Bersch*, 519 F.2d at 993). A federal court also has jurisdiction under the "effects" test where illegal activity abroad causes a "substantial effect" within the United States. *See Consolidated Gold Fields PLC v. Minorco, S.A.*, 871 F.2d 252, 261-62 (2d Cir. 1989). As we find that the allegations are sufficient to show that there is jurisdiction under the conduct test, we reverse.

In employing the conduct test, Judge Friendly wrote that subject matter jurisdiction could be based upon the "perpetration of fraudulent acts themselves [but] does not extend to mere preparatory activities or the failure to prevent fraudulent acts where the bulk of the activity was performed in foreign countries, such as in *Bersch*." *ITT v. Vencap, Ltd.*, 519 F.2d 1001, 1018 (2d Cir. 1975). In *Psimenos*, we held that lawsuits by aliens alleging securities fraud should be entertained in American courts "only where conduct material to the completion of the fraud occurred in the United States." 722 F.2d at 1046. In this case, we find that the negotiations with and sales to American Continental and Al-Turki constituted conduct resulting in the consummation of the securities law fraud.

We disagree with the district court's finding that "nothing further had to be done to complete the fraud after plaintiffs paid for their SEIC shares in reliance upon the prospectus." 751 F. Supp. at 1118. Plaintiffs, except Alfadda, purchased their shares in April 1984. The sales to Lincoln and Al-Turki were not finalized until June. Thus, the prospectuses did not become fraudulent until additional voting shares were sold to Lincoln and Al-Turki. At the very least, the negotiations and communications of Radwan, Fenn and Reilly with American Continental officers and Al-Turki constituted "conduct material to the completion of the fraud . . . ", *Psimenos*, 722 F.2d at 1046, and hence are a basis for subject matter jurisdiction.

The fact that American Continental's investment was structured so that its subsidiary, Lincoln American Investments, a Netherlands Antilles shell company created for the purpose of holding the SEIC shares, was the nominal purchaser does not detract from the import of the

United States meetings and negotiations which preceded the sale. *See* Restatement (Second) of Foreign Relations Law of the United States § 416(d) (1987) ("The United States may generally exercise jurisdiction to prescribe with respect to conduct occurring predominantly in the United States that is related to a transaction in securities, even if the transaction takes place outside the United States."). Defendants also argue that Al-Turki negotiated for and decided to purchase SEIC stock while in several non-United States locations prior to the June telexes Al-Turki received in Houston. However, in the district court, Al-Turki averred that "[a]s of June 22, 1984, I had not agreed to participate in the SEIC Stock Offering." The district court did not resolve this factual dispute. Viewing the evidence in the light most favorable to the plaintiffs, as we must on appeal of the dismissal of a complaint for lack of subject matter jurisdiction, we find that negotiations for the sale of SEIC stock to Al-Turki transpired in Houston in late June.

The district court also dismissed plaintiffs' RICO claims for lack of subject matter jurisdiction. Like the Securities Exchange Act, the RICO statute is silent as to its extraterritorial application. Thus, we must ascertain whether Congress would have intended that federal courts should be concerned with specific international controversies. *See* Brilmayer, *The Extraterritorial Application of American Law: A Methodological and Constitutional Appraisal*, 50 Law & Contemp. Probs. 11, 14 nn. 18-21 (Summer 1987) (collecting cases).

Relative to subject matter jurisdiction for international securities transactions, there is a dearth of Second Circuit precedent regarding the extraterritorial application of RICO. However, in *United States v. Parness*, 503 F.2d 430 (2d Cir. 1974), *cert. denied*, 419 U.S. 1105 (1975),

we rejected arguments circumscribing RICO's extra-territorial application to foreign enterprises:

> On its face the proscription [against acquiring an "enterprise"] is all inclusive. It permits no inference that the [RICO] Act was intended to have a parochial application. The legislative history, moreover, indicates the intent of Congress that this provision be broadly construed . . . . In short, we find no indication that Congress intended to limit Title IX [RICO] to infiltration of domestic enterprises. On the contrary, the salutary purposes of the Act would be frustrated by such construction.

Id. at 439. The mere fact that the corporate defendants are foreign entities does not immunize them from the reach of RICO.

As the Supreme Court has stated, "the heart of any RICO complaint is the allegation of a *pattern* of racketeering activity." *Agency Holding Corp. v. Malley-Duff & Associates, Inc.*, 483 U.S. 143, 154 (1987) (emphasis in original). Among the predicate acts alleged by plaintiffs are the securities fraud violations consummated by the sales of SEIC shares to Lincoln American Investments and Al-Turki. Reilly and defendants Radwan and Fenn, all American citizens, participated in many of the United States communications and negotiations preceding the sales. Nevertheless, the district court dismissed the RICO claims because it considered these predicate acts to "constitute the after-the-event working out of an already completed fraud. . . ." 751 F. Supp. at 1121. As discussed *supra*, we disagree with the district court's holding that the alleged fraud was complete upon delivery of the misrepresentations contained in the prospectuses and the subsequent purchases of SEIC stock by plaintiffs Abbar,

Zainy and the Kanoos in April 1984. The sales to Lincoln American Investments and Al-Turki were predicate acts which occurred primarily in the United States, and hence, serve as a basis of subject matter jurisdiction for the RICO claims.

Reversed and remanded for further proceedings.

Opinion of the Southern District of New York

UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

89 Civ. 6217 (LMM)

ABDULAZIZ A. ALFADDA, ABDULLAH ABBAR, ABDULLA KANOO, ABDULAZIZ KANOO, YUSIF BIN AHMED KANOO (a Partnership Company), and AHMED A. ZAINY,

Plaintiffs,

—against—

RICHARD A. FENN, JAMAL RADWAN, SAUDI EUROPEAN INVESTMENT CORPORATION N.V., SAUDI EUROPEAN BANK, S.A., ALEF INVESTMENT CORPORATION N.V., and ALEF BANK, S.A.,

Defendants.

OPINION AND ORDER

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MCKENNA, D.J.

Plaintiffs, five individual foreign nationals and one foreign partnership company, brought this action for violations of the Racketeer Influenced and Corrupt Organizations Act ("RICO"), 18 U.S.C. §§ 1961-68 (Count I), for violations of Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b), and Rule 10b-5 of the Securities and Exchange Commission, 17 C.F.R. § 240.10b-5 (Count II; plaintiff Alfadda does not join in this Count), and for common law fraud, breach of fiduciary duty and rescission of contract. Plaintiffs premise their amended complaint upon their purchase of shares of stock through private placements. Defendants have moved to dismiss the amended complaint for lack of subject matter jurisdiction or on the ground of

forum non conveniens.[1] Defendants have also moved to have the fraud claims dismissed for failure to plead fraud with particularity. For the reasons stated below, the amended complaint is dismissed for lack of subject matter jurisdiction.

BACKGROUND

Defendant Saudi European Investment Corporation N.V. ("SEIC") is a closely held Netherlands Antilles company which operated as a holding and/or controlling company of the other corporate defendants, Saudi European Bank S.A. ("SE Bank") (now known as Societe de Banque Privee), a French bank, Alef Investment Corporation N.V. ("AIC"), a Netherlands Antilles corporation, and Alef Bank S.A. ("Alef Bank"), a French bank (collectively, the "SE Group"). The individual defendants, Jamal Radwan ("Radwan") and Richard Fenn ("Fenn") are United States citizens who are sued based upon their activities in connection with the corporate defendants.

The amended complaint alleges that on or about February 4, 1979 defendant Radwan invited plaintiff Alfadda to become a shareholder in a proposed company, SEIC. SEIC was to have 40,000 authorized shares of stock and the original stock offering would consist of 20,000 shares at a price of $1,000 per share. In July 1979, Alfadda purchased 1000 shares of SEIC voting stock for $1,000,000. Pursuant to the terms of the offering, Alfadda and the other holders of the original 20,000 shares sold were to be given a preference in the offering of new shares, in proportion to the number of original shares held by them.

Around October 1983, the defendants planned a second offering of SEIC stock. The original shares sold were to be subject to a 30 for 1 split, creating 600,000 shares. The prospectus for the second offering stated that another 600,000

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1 The complaint was amended after defendants' motion to dismiss was filed and plaintiffs had had an opportunity for discovery directed to jurisdictional issues; the parties then argued the motion in light of the allegations of the complaint as amended.

voting shares (which represented the 20,000 shares which were not issued in the original offering split 30 for 1) were to be sold at $100 per share. In the event of an oversubscription, up to 1,800,000 non-voting shares were to be issued.

Plaintiffs allege that, despite the representations made in the prospectus upon which they relied, 1,200,000 voting shares were sold, diluting their interests. Plaintiff Alfadda claims that, despite his reliance upon the representations made to him when he purchased shares in the original offering, defendants never informed him of the second offering, thus depriving him of his preferential right to purchase new shares.

In addition, plaintiffs' RICO, breach of fiduciary duty, and common law fraud claims allege that the defendants diverted proceeds from the oversubscription of stock for their personal benefit and the benefit of certain favored SEIC shareholders, and that the defendants used United States mail, telephone and wire services to further their scheme and conceal their activities.

Plaintiffs allege conduct by the defendants claimed to be relevant to subject matter jurisdiction. Plaintiffs specifically assert the following: defendants hired Ronald Reilly, a United States citizen, and his company, Capital International, Inc., to help prepare and market the second offering, and he performed some of his functions in the United States; SEIC's general counsel, Mario Diaz-Cruz, Esq., assisted in the preparation of the offering in New York; shares were sold in the United States to Lincoln American Investments N.V. ("Lincoln"), a Netherlands Antilles subsidiary of American Continental Corporation ("ACC"), and to a foreign businessman, Abdulrahaman Al-Turki;[2] defendants repeatedly used United States mail, wire and telephone services; stock certificates were printed in New York and sent abroad; moneys used to purchase the shares were deposited in United States banks;

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2 Mr. Al-Turki is a plaintiff in a subsequent action filed in this Court in which allegations similar to those made in the present case are made. *Al-Turki, et al. v. Fenn, et al.*, S.D.N.Y. 90 Civ. 4470 (LMM). A second related case is *Resolution Trust Corporation, etc., et al. v. Fenn, et al.*, S.D.N.Y. 90 Civ. 6050 (LMM), involving the ACC transaction.

meetings between representatives of ACC and the defendants were held in Washington, D.C. and Florida to assuage ACC and Al-Turki after they discovered and objected to the dilution of their interests; and the defendants purchased, with funds diverted from the proceeds of the oversubscription, one United States company and stock in another.

SECURITIES LAW VIOLATIONS

The availability of authority suggests that plaintiffs' securities law claims (Count II) be considered before their RICO claim (Count I). The Second Circuit has considered the application of the federal securities laws to transnational transactions in a line of detailed decisions: *Schoenbaum v. Firstbrook*, 405 F.2d 200, *modified on other grounds* (*en banc*), 405 F.2d 215 (1968), *cert. denied*, 395 U.S. 906, 89 S.Ct. 1747, 23 L.Ed.2d 219 (1969); *Leasco Data Processing Equipment Corp. v. Maxwell*, 468 F.2d 1326 (1972); *Bersch v. Drexel Firestone. Inc.*, 519 F.2d 974, *cert. denied*, 423 U.S. 1018, 96 S.Ct. 453, 46 L.Ed.2d 389 (1975); *IIT v. Vencap, Ltd.*, 519 F.2d 1001 (1975); *Fidenas AG v. Compagnie Internationale*, 606 F.2d 5 (1979); *IIT v. Cornfeld*, 619 F.2d 909 (1980); *Psimenos v. E.F. Hutton & Co.*, 722 F.2d 1041 (1983); *AVC Nederland B.V. v. Atrium Inv. Partnership*, 740 F.2d 148 (1984); and *Consolidated Goldfields PLC v. Minorco*, 871 F.2d 252, *cert. dismissed*, 110 S.Ct. 29 (1989).[3] In these cases, the Second Circuit developed two tests for determining when federal securities laws apply extraterritorially: the "conduct test," which looks to whether substantial conduct directly causing injuries to foreign plaintiffs takes place in this country; and the "effects test," which looks to whether conduct outside the country results in substantial and specific deleterious effects here. The conduct and effects tests are used to determine presumed Congressional intent as to extraterritorial application. In cases in which the securities

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3 The late Judge Henry J. Friendly wrote the opinions for the court in *Leasco*, *Bersch*, the two *IIT* cases, and *AVC Nederland*.

laws are found not to have been intended to apply extraterritorially, subject matter jurisdiction does not exist.[4]

The Second Circuit considered both tests in *Bersch v. Drexel Firestone, Inc.*, 519 F.2d 974 (2d Cir. 1975), *supra*. There, purchasers of common stock in a Canadian corporation brought suit as a class for violations of the securities laws and for common law fraud. Plaintiffs alleged that they relied on misleading prospectuses. The class included some Americans, but consisted predominantly of foreign nationals. The court held that where the conduct in the United States is merely preparatory, takes the form of culpable non-feasance, or is relatively inextensive in comparison to the extent of conduct abroad, there is no subject matter jurisdiction over a suit brought by foreign plaintiffs. 519 F.2d at 987.

While the *Bersch* court dismissed the claims of the foreign plaintiffs because of the insufficiency of the relevant conduct within the United States, it sustained subject matter jurisdiction over the claims of American plaintiffs under the effects test. The court explained that, regardless of whether or not acts of material importance occurred in the United States, the exercise of jurisdiction was warranted as to those plaintiffs because of the detrimental effects in the United States felt by United States citizens. *Id.* at 991.

Under the *Bersch* analysis, plaintiffs' claims for securities fraud must be dismissed. In *Bersch*, the court characterized the following as merely preparatory:

> . . . representatives of IOS, the major underwriters in the Drexel Group, their attorneys and accountants met in New York on numerous occasions to initiate, organize and structure the offering; that a New York law firm was retained to represent the underwriters and had

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4 The principal inquiry is whether, where a statute is silent as to its extraterritorial application, Congress intended it to apply to the transnational activity in question. *See* Brilmayer, *The Extraterritorial Application of American Law: A Methodological and Constitutional Appraisal*, 50 *Law and Contemporary Problems*, (1987) 11, at 14 nn. 18-21 (collecting cases). Some courts have held that legislation is presumed to apply only to events occuring within the United States. *Id.* at 15n. 23 (collecting cases).

> numerous meetings with IOS; that Drexel officials and counsel met with the SEC; that the underwriters retained Price Waterhouse & Co. in New York as accountants to assist in reviewing the operations of IOS and received reports from that firm there; that on one occasion Andersen representatives met in New York with the underwriters to explain why Andersen could not perform a full audit for the period January 1-June 30, 1969, within the time allotted and to discuss the amount of work that Andersen might be able to complete during that period; that preliminary discussions on underwriting discounts and commissions possibly took place in New York in July and August, 1969; that parts of the prospectus were drafted in New York and read over the phone to Geneva; that prospective underwriters were shown a draft of the prospectus in New York; and that accounts for the proceeds of the underwriting were opened at the Bank of New York and the proceeds in dollars were to be deposited there pending remittance to IOS.

Id. at 985 n. 24. All of the jurisdictionally relevant conduct alleged here by plaintiffs, taken together, is less than was found to be insufficient to sustain jurisdiction in *Bersch*.

Clarifying what type of conduct is more than merely preparatory, Judge Friendly wrote for the court that the fraud "was committed by placing the allegedly false and misleading prospectus in the purchasers' hands". *Id.* at 987. Here, it is uncontroverted that the prospectus was sent to the plaintiffs from Paris or Geneva, or hand delivered in Saudi Arabia or Bahrain.

Plaintiffs' reliance on *Psimenos v. E. F. Hutton & Co., Inc.*, 722 F.2d 1041 (2d. Cir. 1983), *supra*, is misplaced. In *Psimenos*, a Greek citizen opened a commodities trading account with the Athens office of E. F. Hutton. The plaintiff suffered losses because of trades made on his behalf on United States commodities markets. While the court found that most of the fraudulent misrepresentations occurred outside the United States, it held that the fraud was consum-

mated in this country, observing that "[t]rading activities on United States commodities markets were significant acts without which Psimenos' losses would not have occurred and are sufficient to establish jurisdiction." *Id.* at 1048. The *Psimenos* court stressed that the commodities contracts were domestic contracts, domestically regulated and comparable to "securities of a United States corporation traded in the United States." *Id.* at 1047.

Here, by contrast, SEIC is a foreign corporation whose stock is not registered with any domestic exchange. Moreover, while in *Psimenos* the fraud could not have been completed without the trades in New York on the commodities markets, in this case nothing further had to be done to complete the fraud after plaintiffs paid for their SEIC shares in reliance upon the prospectus. As in *Bersch*, the fraud was perpetrated by placing the misleading prospectus into the plaintiffs' hands outside the United States.

Plaintiffs also argue that the prospectus emanated, as did the misleading pamphlet in *Psimenos*, from the United States, and that jurisdiction, therefore, should be sustained. To support their argument plaintiffs insist that the prospectus was prepared in the United States. Defendants, however, maintain that it was prepared in Paris.

The Court has authority to resolve factual disputes when a party moving to dismiss for lack of subject matter jurisdiction attacks the substance of the jurisdictional allegations. *Thornhill Pub. v. General Telephone & Electronics*, 594 F.2d 730, 733 (2d Cir. 1979). *See* 5A C. Wright & A. Miller, *Federal Practice & Procedure* § 1350 (1990). Both sides have submitted evidence supporting their positions. While it is clear from this evidence that *some* work was done in the United States, much of the evidence, including the deposition testimony of Ronald Reilly and supporting documentation, points to Paris as the location where most of the production of the prospectus took place. The Court finds that the prospectus was prepared primarily outside the United States, and cannot be said to have emanated from here.

Moreover, even if the Court were convinced that the prospectus had emanated from the United States, that, by itself,

would not be enough to confer jurisdiction. *Psimenos*, 722 F.2d at 1046. As stated in *Bersch*, the fraud is committed by placing the allegedly fraudulent prospectus in the plaintiffs' hands. 519 F.2d at 987. As already noted, plaintiffs received the prospectus outside the United States.

Plaintiffs contend that jurisdiction can also be sustained under the effects test. As articulated in *Schoenbaum v. Firstbrook*, *supra*, the effects test will confer jurisdiction over a claim involving acts done outside the United States but producing effects within it. 405 F.2d 200, 206 (2d Cir. 1968) ("We believe that Congress intended the Exchange Act to have extraterritorial application in order to protect domestic investors who have purchased foreign securities on American exchanges and to protect the domestic securities market from the effects of improper foreign transactions in American securities.") Contrary to plaintiffs' contentions, the effects test is inapplicable here. These plaintiffs are not "domestic investors" nor are the securities at issue traded on any domestic exchange.

Plaintiffs argue that the second offering was "predominantly American" because of the large number of shares allegedly sold in the United States to Lincoln and Al-Turki. If these two purchasers were indeed American investors, as plaintiffs claim, and they suffered injury from acts done outside the United States, then, *arguendo*, the exercise of jurisdiction over their claims might be justified.[5] Foreign plaintiffs, however, cannot sustain their claims on the basis that American investors have cognizable claims. In *Bersch*, the court severed the claims of the foreign plaintiffs from those of the Americans and held jurisdiction to exist under the effects test only over the Americans' claims. 519 F.2d at 990-992. Thus, the Court does not have jurisdiction over the claims of the plaintiffs under the effects test.

The other Second Circuit decisions cited at pages 5-6 above will not support subject matter jurisdiction over plaintiffs' securities law claims. In *Fidenas*, the Second Circuit decided

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5 Defendants have not moved to dismiss the related cases cited in footnote 2, *supra*, and nothing contained in this opinion is intended to express a view as to those cases.

that jurisdiction did not exist because the transactions were predominantly foreign, all the parties were foreign and any domestic activity was secondary and ancillary. The cases in which jurisdiction was sustained either involved conduct in the United States sufficient to confer jurisdiction, as in *Leasco* (material misrepresentations made in and sent to the United States and defrauded purchaser a wholly owned subsidiary of an American company whose stock was listed on the New York Stock Exchange); *Cornfeld* (transactions were fully consummated in the United States and securities at issue were securities of American corporations); and *AVC Nederland* (representations made and negotiations conducted in the United States and investments at issue involved American real estate owned by partnership formed in accordance with American law by two foreigners); or losses suffered by Americans as in *Minorco* (American residents represented 2.5% of the plaintiff corporation's shareholders).

RICO VIOLATIONS

Plaintiffs allege that the SE Group (or SEIC) constitutes an enterprise within the meaning of RICO and that defendants have engaged in a pattern of racketeering activity which includes as predicate acts the securities fraud discussed above, as well as uses by defendants of the United States mails, wire communications, and transportation of money in interstate commerce, in violation of 18 U.S.C. §§ 1341, 1343 and 2314. The amended complaint states that the defendants used income derived from the pattern of racketeering activity to operate the SE Group (or SEIC) in violation of 18 U.S.C. § 1962(a); that defendants have acquired or maintained an interest in or control of the SE Group in violation of 18 U.S.C. § 1962(b); that defendants have conducted or participated in the conduct of the SE Group (or SEIC) in violation of 18 U.S.C. § 1962(c); and that defendants have conspired with each other in conducting the affairs of the SE Group (or SEIC) in violation of 18 U.S.C. § 1962(d). Because the alleged conduct took place only partly in the United States,

the court must determine whether jurisdiction exists over the RICO claims.

The application of RICO to transnational transactions has not yet been explored with the thoroughness with which the Second Circuit has considered the extraterritorial application of the securities laws. The only Second Circuit decision on the subject cited by plaintiffs is *United States v. Parness*, 503 F.2d 430 (2d Cir. 1974). In *Parness*, however, the pattern of racketeering activity took place almost entirely within the United States and the question was whether the acquisition of a foreign company with illegally obtained funds violated the statute. The Second Circuit held that RICO prohibited acquiring a foreign company with funds obtained through predicate conduct within the United States. The court pointed out that a contrary construction of RICO "would permit those whose actions ravage the American economy to escape prosecution simply by investing the proceeds of their ill-gotten gains in a foreign enterprise." 503 F.2d at 439. Here, however, the "ill-gotten gains" are the moneys obtained by defendants from foreign nationals, and it is, if the allegations of the amended complaint are correct, the economies of Saudi Arabia and Bahrain, not that of the United States, that may be claimed to have been "ravaged."

The question before this Court is whether there is subject matter jurisdiction over a RICO claim where some but not all of the alleged predicate conduct took place within the United States, where the underlying fraud to which those predicate acts relate took place outside the United States and where the cognizable damages occur to foreign nationals outside the United States.

Although the question was not articulated as such, it was implicitly presented to the Ninth Circuit in *Republic of the Philippines v. Marcos*, 862 F.2d 1355 (9th Cir. 1988) (*en banc*), also relied on by plaintiffs. *Marcos* involved a RICO claim to the effect that Ferdinand and Imelda Marcos plundered the Philippines and then invested some of the funds thus obtained in the United States. Among the predicate acts which constituted the pattern of racketeering were instances of mail and wire fraud occurring in United States territory

and the transportation of stolen property across international borders. Sustaining jurisdiction, the Ninth Circuit wrote: "The criminal enterprise which [the Marcoses] are charged with conducting consisted in operations taking place within the United States. These operations had multiple effects on the domestic and foreign commerce of this country." *Id.* at 1358.

Under the Ninth Circuit analysis, subject matter jurisdiction over this case would probably be sustained. As in *Marcos*, the pattern of racketeering alleged by the plaintiffs includes instances of mail and wire fraud within the United States and the transportation in commerce of fraudulently obtained property.

However, the Court doubts that the Second Circuit would, in a case such as this one, extend the extraterritorial application of RICO as far as the Ninth Circuit did in *Marcos*. The Second Circuit's standard for the extraterritorial application of federal securities law is more restrictive than that of the Ninth and other Circuits. The Second Circuit requires that the acts performed in the United States directly cause the losses to foreign plaintiffs. *See Bersch*, *supra*, 519 F.2d at 993 (federal securities laws do not "apply to losses from sales of securities to foreigners outside the United States unless acts . . . within the United States directly caused such losses."); *IIT v. Vencap*, 519 F.2d 1001, 1018 (2d Cir. 1975), *supra*; *see also Zoelsch v. Arthur Andersen & Co.*, 824 F.2d 27 (D.C. Cir. 1987) (comparing the standards set by various Circuits and adopting the Second Circuit's as "the most restrictive"). The Ninth Circuit, on the other hand, only requires that significant acts in furtherance of the fraud take place in the United States. *Grunenthal GmbH v. Hotz*, 712 F.2d 421 (9th Cir. 1983). By analogy to the Second Circuit's standard in the securities law context, the Court concludes that the standard for applying RICO extraterritorially in this Circuit is more restrictive than that in the Ninth, and the Court declines to follow *Marcos*.

The standards within this Circuit for applying United States securities laws and RICO to transnational transactions—at least when RICO is asserted, as here, to

recover for what at bottom is a securities fraud—should be consistent. In finding subject matter jurisdiction over RICO claims in *Parness*, *supra*, the Second Circuit looked, *inter alia*, to the securities law analogy, citing *Leasco*, *supra*, where, it said, "in dealing with one of the antifraud provisions of the Securities Exchange Act of 1934, 15 U.S.C. § 78(j)(b) (1970), we have held that, where there is substantial United States activity and Americans are hurt, it is immaterial that the corporation is foreign." 503 F.2d at 440.

Denial of subject matter jurisdiction over plaintiffs' RICO claim is also consistent with the provisions of the American Law Institute's Restatement, to which the Second Circuit has looked in the securities law context. *See Leasco*, *Bersch*, *Vencao*, *AVC Nederland*, and *Minorco*, *supra*. The Restatement standards are equivalent to the conduct and effects tests developed in the Second Circuit securities law cases. "[A] state has jurisdiction to prescribe law with respect to (1)(a) conduct that, wholly or in substantial part, takes place within its territory; . . . (c) conduct outside its territory that has or is intended to have substantial effect within its territory; . . ." Restatement (Third), The Foreign Relations Law of the United States § 402 (1986). Such jurisdiction, moreover, is subject to a reasonableness limitation, requiring evaluation of, among other things, "the link of the activity to the territory of the regulating state, *i.e.*, the extent to which the activity takes place within the territory, or has substantial, direct, and foreseeable effect upon or in the territory," and "the connections, such as nationality, residence or economic activity, between the regulating state and the person principally responsible for the activity to be regulated, or between that state and those whom the regulation is designed to protect." *Id.* § 403. As has been seen, the facts of the present case do not meet these standards. The principal activity complained of—the communication of fraudulent representations—took place outside of the United States, and the effects of that activity were felt by foreign nationals outside of the United States. Four of the six defendants alleged to be responsible for the plaintiffs' loss are foreign entities and one, Jamal Radwan, while a citizen of the United States, appears from

all of the materials submitted to be a resident of France, not of the United States. Defendant Fenn's American citizenship and residence are not enough to outweigh the foreign connections of the plaintiffs and the other defendants on the Restatement's reasonableness scale.

It is, of course, true that plaintiffs allege predicate activity within the United States. Amended Complaint ¶ 107. Much of it is preparatory to the fraudulent sales to plaintiffs, and the balance is largely related to the alleged concealment of the fraud. Some of it relates to the sales to Mr. Al-Turki and to Lincoln. Such activity, however, is subsidiary to the securities fraud upon plaintiffs which, they assert, was the "essence of defendants' scheme," which "was to represent to investors such as the plaintiffs that SEIC and the SE Group intended to operate the Corporate Defendants as *bona fide* businesses in the manner represented in the Prospectus; in fact, Radwan's and Fenn's true intention was to employ the SE Group, SEIC and their affiliated enterprises as vehicles for self-dealing and fraud." *Id.* ¶ 27. The structure of RICO is such that it will no doubt often be possible to include in a RICO complaint challenging a transnational transaction some subsidiary predicate acts taking place in the United States. Where, however, as here and in so many RICO cases, the heart of the claim is fraud in the sale of securities, there is no basis for thinking that Congress intended predicate acts which are either preparatory, or constitute the after-the-event working out of an already completed fraud, to confer otherwise nonexistent subject matter jurisdiction.

Therefore, the Court holds that when the RICO predicate acts occuring in the United States consist of subsidiary uses of United States communications and transportation systems, but the underlying fraud occurs outside the United States, the Court lacks subject matter jurisdiction over the RICO claim. The tail should not wag the dog. The law in the Second Circuit is that subject matter jurisdiction over the plaintiffs' underlying securities fraud claims does not exist. Consequently, jurisdiction over the RICO claims, which are primarily predicated upon the securities fraud claims, does not exist either. Conduct more substantial than that alleged here must

take place in the United States for RICO jurisdiction to be sustained.

Plaintiffs argue that Congress does not want the United States to be used as a base for manufacturing and exporting fraudulent securities schemes. They are correct. Congress does not. *IIT v. Vencap., supra*, 519 F.2d at 1017. Their securities fraud and RICO claims, however, do not assert claims in which the United States was used as the operating base for the exportation of fraudulent schemes. Rather, the base of operations in this case was outside the United States, and the actions taken here were subsidiary.

The Second Circuit observed in *Bersch*:

> When, as here, a court is confronted with transactions that on any view are predominantly foreign, it must seek to determine whether Congress would have wished the precious resources of the United States Courts and law enforcement agencies to be devoted to them rather than leave the problem to foreign countries.

519 F.2d at 985. This Court does not believe that Congress would have wished the limited judicial resources of the United States to be expended on litigating RICO claims where the domestic conduct amounts to subsidiary uses of the United States communications and transportation systems.

If the Court were to hold otherwise, then jurisdiction could be sustained over a foreign plaintiff's RICO claim solely because the RICO defendants made, say, two telephone calls within the United States, or used the United States mails on two occasions. Given the vast number of foreign and transnational business transactions in which United States mails, wire and telephone systems are used merely by happenstance, United States courts could become flooded with countless foreign based RICO claims bearing little or no nexus to this country. While it is no doubt true that implementation of RICO has exceeded Congress' original vision of the statute (*see generally*, Lynch, *RICO: The Crime of Being A Criminal*, 87 Colum. L. Rev. 661, 920 (1987)), plaintiffs have cited nothing in either the statutory language or its legislative history to indicate that Congress would consider it desirable to

apply RICO to expand the jurisdiction of the federal courts so prodigiously.

PENDENT CLAIMS

All plaintiffs, and all defendants except Fenn, a citizen of New York, and Radwan, who may not be a citizen of any state, are aliens. In the absence of subject matter jurisdiction over plaintiffs' claims asserted under statutes of the United States, their remaining state law claims are dismissed as well. *Philan Ins. Ltd. v. Frank B. Hall & Co., Inc.*, 712 F. Supp. 339 (S.D.N.Y. (989) (Walker, J.), at 345-346.

THE BOND ORDER

By order dated May 10, 1990, the Judge to whom this case was previously assigned required plaintiffs to post a bond in the sum of $300,000 in connection with their conduct of discovery of jurisdictional facts. The order was entered pursuant to Fed. R. Civ. P. 26, and was clearly prompted by a concern that plaintiffs might use liberal federal discovery procedures to obtain information for use in litigation pending outside the United States. Plaintiffs have moved for reconsideration of that order. Subsequent to the order, plaintiffs deposited 5000 shares of SEIC stock with the Clerk of the Court. The Court finds that plaintiffs did not abuse the jurisdictional discovery afforded them, and the Clerk will return the shares to them. Defendants have argued that the bond should also be available to satisfy any judgment obtained by them for costs and any possible order imposing sanctions. The order, however, by its terms, related only to discovery, as its explicit reference to Fed. R. Civ. P. 26 makes clear, and sanctions, in any event, are not warranted.

In view of such direction and the disposition of defendants' motion to dismiss, the motion for reconsideration is DENIED as moot.

CONCLUSION

For the reasons stated above, defendants' motion to dismiss the complaint for lack of subject matter jurisdiction is GRANTED. The Court accordingly finds it unnecessary to consider defendants' motions to dismiss the fraud claims for failure to plead fraud with particularity and to dismiss the complaint on the grounds of *forum non conveniens*. The complaint was amended subsequent to defendants' challenge to subject matter jurisdiction and after discovery of jurisdictional facts, and the amended complaint alleges facts claimed to be relevant to subject matter jurisdiction in great detail. There is, accordingly, no warrant for giving plaintiffs leave to replead.

Plaintiffs motion for reconsideration of the bond order is DENIED as moot. The Clerk is directed to return to plaintiffs' authorized representatives all shares of SEIC stock previously deposited.

The amended complaint is DISMISSED.

SO ORDERED

Dated: New York, New York
November 26, 1990

LAWRENCE M. MCKENNA
Lawrence M. McKenna
U.S.D.J.

Order Denying Suggestion for Rehearing In Banc

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

Docket Number 90-9129

At a stated term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse in the City of New York, on the sixteenth day of July, one thousand nine hundred and ninety-one.

ABDULAZIZ A. ALFADDA; ABDDULLAH ABBAR; ABDULLA KANOO: ABDULAZIZ KANOO; YUSIF BIN AHMED KANOO (A PARTNERSHIP COMPANY); and AHMED A. ZAINY,

Plaintiffs-Appellants,

v

RICHARD A. FENN; JAMAL RADWAN; SAUDI EUROPEAN INVESTMENT CORPORATION, N.V.; SAUDI EUROPEAN BANK, S.A.; ALEF INVESTMENT CORPORATION N.V.; and ALEF BANK S.A.

Defendants-Appellees.

A petition for rehearing containing a suggestion that the action be reheard in banc having been filed herein by Appellees, Richard A. Fenn, Jamal Radwan, Saudi European Investment Corporation N.V., Saudi European Bank, S.A., Alef Investment Corporation N.V., and Alef Bank, S.A.

Upon consideration by the panel that heard the appeal, it is

Ordered that said petition for rehearing is DENIED.

It is further noted that the suggestion for rehearing in banc has been transmitted to the judges of the court in regular active service and to any other judge that heard the appeal and that no such judge has requested that a vote be taken thereon.

ELAINE B. GOLDSMITH

Elaine B. Goldsmith
Clerk

Judgment of the Second Circuit

UNITED STATES COURT OF APPEALS
FOR THE SECOND CIRCUIT

Docket No. 90-9129

At a stated Term of the United States Court of Appeals for the Second Circuit, held at the United States Courthouse in the City of New York, on the 5th day of June, one thousand nine hundred and ninety-one.

Present: HON. J. EDWARD LUMBARD,
HON. WILFRED FEINBERG,
HON. JOSEPH M. MCLAUGHLIN,
Circuit Judges.

ABDULAZIZ A. ALFADDA, ABDULLAH ABBAR, ABDULLA KANOO, ABDULAZIZ KANOO, YUSIF BIN AHMED KANOO (a partnership company), and AHMED A. ZAINY,

Plaintiffs-Appellants,

—against—

RICHARD A. FENN, JAMAL RADWAN, SAUDI EUROPEAN INVESTMENT CORPORATION, N.V., SAUDI EUROPEAN BANK, S.A., ALEF INVESTMENT CORPORATION N.V., and ALEF BANK, S.A.

Defendants-Appellees.

Appeal from the United States District Court for the Southern District of New York.

This cause came on to be heard on the transcript of record from the United States District Court for the Southern District of New York, and was argued by counsel.

ON CONSIDERATION WHEREOF, it is now hereby ordered, adjudged and decreed that the appeal from the order of said district court be and it hereby is reversed and the action be and it hereby is remanded to the said district court for further proceedings in accordance with the opinion of this court with costs to be taxed against the appellee.

Elaine B. Goldsmith,
Clerk

by: EDWARD J. GUARDARO
Edward J. Guardaro,
Deputy Clerk

Statutory Provisions Involved

United States Code

Title 18

Racketeer Influenced and Corrupt Organizations Act

§ 1961. Definitions

As used in this chapter—

(1) "racketeering activity" means (A) any act or threat involving murder, kidnaping, gambling, arson, robbery, bribery, extortion, dealing in obscene matter, or dealing in narcotic or other dangerous drugs, which is chargeable under State law and punishable by imprisonment for more than one year; (B) any act which is indictable under any of the following provisions of title 18, United States Code: Section 201 (relating to bribery), section 224 (relating to sports bribery, sections 471, 472, and 473 (relating to counterfeiting), section 659 (relating to theft from interstate shipment) if the act indictable under section 659 is felonious, section 664 (relating to embezzlement from pension and welfare funds), sections 891-894 (relating to extortionate credit transactions), section 1029 (relating to fraud and related activity in connection with access devices), section 1084 (relating to the transmission of gambling information), section 1341 (relating to mail fraud), section 1343 (relating to wire fraud), section 1344 (relating to financial institution fraud), sections 1461-1465 (relating to obscene matter), section 1503 (relating to obstruction of justice), section 1510 (relating to obstruction of criminal investigations), section 1511 (relating to the obstruction of State or local law enforcement), section 1512 (relating to tampering with a witness, victim, or an informant), section 1513 (relating to retaliating against a witness, victim, or an informant), section 1951 (relating to interference with commerce, robbery, or extortion), section 1952 (relating

to racketeering), section 1953 (relating to interstate transportation of wagering paraphernalia), section 1954 (relating to unlawful welfare fund payments), section 1955 (relating to the prohibition of illegal gambling businesses), section 1956 (relating to the laundering of monetary instruments), section 1957 (relating to engaging in monetary transactions in property derived from specified unlawful activity) sections 2251 through 2252 (relating to sexual exploitation of children), section 1958 (relating to use of interstate commerce facilities in the commission of murder-for-hire), sections 2312 and 2313 (relating to interstate transportation of stolen motor vehicles), sections 2314 and 2315 (relating to interstate transportation of stolen property), section 2321 (relating to trafficking in certain motor vehicles or motor vehicle parts), sections 2341-2346 (relating to trafficking in contraband cigarettes), sections 2421-24 (relating to white slave traffic), (C) any act which is indictable under title 29, United States Code, section 186 (dealing with restrictions on payments and loans to labor organizations) or section 501(c) (relating to embezzlement from union funds), (D) any offense involving fraud connected with a case under title 11, fraud in the sale of securities, or the felonious manufacture, importation, receiving, concealment, buying, selling, or otherwise dealing in narcotic or other dangerous drugs, punishable under any law of the United States, or (E) any act which is indictable under the Currency and Foreign Transactions Reporting Act.

(2) "State" means any State of the United States, the District of Columbia, the Commonwealth of Puerto Rico, any territory or possession of the United States, any political subdivision, or any department, agency, or instrumentality thereof;

(3) "person" includes any individual or entity capable of holding a legal or beneficial interest in property;

(4) "enterprise" includes any individual, partnership, corporation, association, or other legal entity, and any

union or group of individuals associated in fact although not a legal entity;

(5) "pattern of racketeering activity" requires at least two acts of racketeering activity, one of which occurred after the effective date of this chapter and the last of which occurred within ten years (excluding any period of imprisonment) after the commission of a prior act of racketeering activity;

(6) "unlawful debt" means a debt (A) incurred or contracted in gambling activity which was in violation of the law of the United States, a State of political subdivision thereof, or which is unenforceable under State of Federal law in whole or in part as to principal or interest because of the laws relating to usury, and (B) which was incurred in connection with the business of gambling in violation of the law of the United States, a State or political subdivision thereof, or the business of lending money or a thing of value at a rate usurious under State or Federal law, where the usurious rate is at least twice the enforceable rate;

(7) "racketeering investigator" means any attorney or investigator so designated by the Attorney General and charged with the duty of enforcing or carrying into effect this chapter;

(8) "racketeering investigation" means any inquiry conducted by any racketeering investigator for the purpose of ascertaining whether any person has been involved in any violation of this chapter or of any final order, judgment, or decree of any court of the United States, duly entered in any case or proceeding arising under this chapter;

(9) "documentary material" includes any book, paper, document, record, recording, or other material; and

(10) "Attorney General" includes the Attorney General of the United States, the Deputy Attorney General

of the United States, the Associate Attorney General of the United States, any Assistant Attorney General of the United States, or any employee of the Department of Justice or any employee of any department or agency of the United States so designated by the Attorney General to carry out the powers conferred on the Attorney General by this chapter. Any department or agency so designated may use in investigations authorized by this chapter either the investigative provisions of this chapter or the investigative power of such department or agency otherwise conferred by law.

§ 1962. Prohibited activities

(a) It shall be unlawful for any person who has received any income derived, directly or indirectly, from a pattern of racketeering activity or through collection of an unlawful debt in which such person has participated as a principal within the meaning of section 2, title 18, United States Code, to use or invest, directly or indirectly, any part of such income, or the proceeds of such income, in acquisition of any interest in, or the establishment or operation of, any enterprise which is engaged in, or the activities of which affect, interstate or foreign commerce. A purchase of securities on the open market for purposes of investment, and without the intention of controlling or participating in the control of the issuer, or of assisting another to do so, shall not be unlawful under this subsection if the securities of the issuer held by the purchaser, the members of his immediate family, and his or their accomplices in any pattern or racketeering activity or the collection of an unlawful debt after such purchase do not amount in the aggregate to one percent of the outstanding securities of any one class, and do not confer, either in law or in fact, the power to elect one or more directors of the issuer.

(b) It shall be unlawful for any person through a pattern of racketeering activity or through collection of an unlawful debt to acquire or maintain, directly or indirectly, any inter-

est in or control of any enterprise which is engaged in, or the activities of which affect, interstate or foreign commerce.

(c) It shall be unlawful for any person employed by or associated with any enterprise engaged in, or the activities of which affect, interstate or foreign commerce, to conduct or participate, directly or indirectly, in the conduct of such enterprise's affairs through a pattern of racketeering activity or collection of unlawful debt.

(d) It shall be unlawful for any person to conspire to violate any of the provisions of subsection (a), (b), (c) of this section.

§ 1963. Criminal penalties

(a) Whoever violates any provision of section 1962 of this chapter shall be fined under this title or imprisoned not more than 20 years (or for life if the violation is based on a racketeering activity for which the maximum penalty includes life imprisonment), or both, and shall forfeit to the United States, irrespective of any provision of State law—

(1) any interest the person has acquired or maintained in violation of section 1962;

(2) any—

(A) interest in;

(B) security of;

(C) claim against; or

(D) property or contractual right of any kind affording a source of influence over;

any enterprise which the person has established, operated, controlled, conducted, or participated in the conduct of, in violation of section 1962; and

(3) any property constituting, or derived from, any proceeds which the person obtained, directly or indirectly, from racketeering activity or unlawful debt collection in violation of section 1962.

The court, in imposing sentence on such person shall order, in addition to any other sentence imposed pursuant to this section, that the person forfeit to the United States all property described in this subsection. In lieu of a fine otherwise authorized by this section, a defendant who derives profits or other proceeds from an offense may be fined not more than twice the gross profits or other proceeds.

(b) Property subject to criminal forfeiture under this section includes—

(1) real property, including things growing on, affixed to, and found in land; and

(2) tangible and intangible personal property, including rights, privileges, interests, claims, and securities.

(c) All right, title, and interest in property described in subsection (a) vests in the United States upon the commission of the act giving rise to forfeiture under this section. Any such property that is subsequently transferred to a person other than the defendant may be the subject of a special verdict of forfeiture and thereafter shall be ordered forfeited to the United States, unless the transferee establishes in a hearing pursuant to subsection (*l*) that he is a bona fide purchaser for value of such property who at the time of purchase was reasonably without cause to believe that the property was subject to forfeiture under this section.

(d)(1) Upon application of the United States, the court may enter a restraining order or injunction, require the execution of a satisfactory performance bond, or take any other action to preserve the availability of property described in subsection (a) for forfeiture under this section—

(A) upon the filing of an indictment or information charging a violation of section 1962 of this chapter and alleging that the property with respect to which the order is sought would, in the event of conviction, be subject to forfeiture under this section; or

(B) prior to the filing of such an indictment or information, if, after notice to persons appearing to have an interest in the property and opportunity for a hearing, the court determines that—

(i) there is a substantial probability that the United States will prevail on the issue of forfeiture and that failure to enter the order will result in the property being destroyed, removed from the jurisdiction of the court, or otherwise made unavailable for forfeiture; and

(ii) the need to preserve the availability of the property through the entry of the requested order outweighs the hardship on any party against whom the order is to be entered:

Provided, however, That an order entered pursuant to subparagraph (B) shall be effective for not more than ninety days, unless extended by the court for good cause shown or unless an indictment or information described in subparagraph (A) has been filed.

(2) A temporary restraining order under this subsection may be entered upon application of the United States without notice or opportunity for a hearing when an information or indictment has not yet been filed with respect to the property, if the United States demonstrates that there is probable cause to believe that the property with respect to which the order is sought would, in the event of conviction, be subject to forfeiture under this section and that provision of notice will jeopardize the availability of the property for forfeiture. Such a temporary order shall expire not more than ten days after the date on which it is entered, unless extended for good cause shown or unless the party against whom it is entered consents to an extension for a longer period. A hearing requested concerning an order entered under this paragraph shall be held at the earliest possible time, and prior to the expiration of the temporary order.

(3) The court may receive and consider, at a hearing held pursuant to this subsection, evidence and information that would be inadmissible under the Federal Rules of Evidence.

(e) Upon conviction of a person under this section, the court shall enter a judgment of forfeiture of the property to the United States and shall also authorize the Attorney General to seize all property ordered forfeited upon such terms and conditions as the court shall deem proper. Following the entry of an order declaring the property forfeited, the court may, upon application of the United States, enter such appropriate restraining orders or injunctions, require the execution of satisfactory performance bonds, appoint receivers, conservators, appraisers, accountants, or trustees, or take any other action to protect the interest of the United States in the property ordered forfeited. Any income accruing to, or derived from, an enterprise or an interest in an enterprise which has been ordered forfeited under this section may be used to offset ordinary and necessary expenses to the enterprise which are required by law, or which are necessary to protect the interests of the United States or third parties.

(f) Following the seizure of property ordered forfeited under this section, the Attorney General shall direct the disposition of the property by sale or any other commercially feasible means, making due provision for the rights of any innocent persons. Any property right or interest not exercisable by, or transferable for value to, the United States shall expire and shall not revert to the defendant, nor shall the defendant or any person acting in concert with or on behalf of the defendant be eligible to purchase forfeited property at any scale held by the United States. Upon application of a person, other than the defendant or a person acting in concert with or on behalf of the defendant, the court may restrain or stay the sale or disposition of the property pending the conclusion of any appeal of the criminal case giving rise to the forfeiture, if the applicant demonstrates that proceeding with the sale or disposition of the property will result in irreparable injury, harm or loss to him. Notwithstanding 31 U.S.C. 3302(b), the proceeds of any sale or other disposi-

tion of property forfeited under this section and any moneys forfeited shall be used to pay all proper expenses for the forfeiture and the sale, including expenses of seizure, maintenance and custody of the property pending its disposition, advertising and court costs. The Attorney General shall deposit in the Treasury any amounts of such proceeds or moneys remaining after the payment of such expenses.

(g) With respect to property ordered forfeited under this section, the Attorney General is authorized to—

(1) grant petitions for mitigation or remission of forfeiture, restore forfeited property to victims of a violation of this chapter, or take any other action to protect the rights of innocent persons which is in the interest of justice and which is not inconsistent with the provisions of this chapter;

(2) compromise claims arising under this section:

(3) award compensation to persons providing information resulting in a forfeiture under this section;

(4) direct the disposition by the United States of all property ordered forfeited under this section by public sale or any other commercially feasible means, making due provision for the rights of innocent persons; and

(5) take appropriate measures necessary to safeguard and maintain property ordered forfeited under this section pending its disposition.

(h) The Attorney General may promulgate regulations with respect to—

(1) making reasonable efforts to provide notice to persons who may have an interest in property ordered forfeited under this section;

(2) granting petitions for remission or mitigation of forfeiture;

(3) the restitution of property to victims of an offense petitioning for remission or mitigation of forfeiture under this chapter;

(4) the disposition by the United States of forfeited property by public sale or other commercially feasible means;

(5) the maintenance and safekeeping of any property forfeited under this section pending its disposition; and

(6) the compromise of claims arising under this chapter.

Pending the promulgation of such regulations, all provisions of law relating to the disposition of property, or the proceeds from the sale thereof, or the remission or mitigation of forfeitures for violation of the customs laws, and the compromise of claims and the award of compensation to informers in respect of such forfeitures shall apply to forfeitures incurred, or alleged to have been incurred, under the provisions of this section, insofar as applicable and not inconsistent with the provisions hereof. Such duties as are imposed upon the Customs Service or any person with respect to the disposition of property under the customs law shall be performed under this chapter by the Attorney General.

(i) Except as provided in subsection (l), no party claiming an interest in property subject to forfeiture under this section may—

(1) intervene in a trial or appeal of a criminal case involving the forfeiture of such property under this section; or

(2) commence an action at law or equity against the United States concerning the validity of his alleged interest in the property subsequent to the filing of an indictment or information alleging that the property is subject to forfeiture under this section.

(j) The district courts of the United States shall have jurisdiction to enter orders as provided in this section without regard to the location of any property which may be subject to forfeiture under this section or which has been ordered forfeited under this section.

(k) In order to facilitate the identification or location of property declared forfeited and to facilitate the disposition of petitions for remission or mitigation of forfeiture, after the entry of an order declaring property forfeited to the United States the court may, upon application of the United States, order that the testimony of any witness relating to the property forfeited be taken by deposition and that any designated book, paper, document, record, recording, or other material not privileged be produced at the same time and place, in the same manner as provided for the taking of depositions under Rule 15 of the Federal Rules of Criminal Procedure.

(*l*)(1) Following the entry of an order of forfeiture under this section, the United States shall publish notice of the order and of its intent to dispose of the property in such manner as the Attorney General may direct. The Government may also, to the extent practicable, provide direct written notice to any person known to have alleged an interest in the property that is the subject of the order of forfeiture as a substitute for published notice as to those persons so notified.

(2) Any person, other than the defendant, asserting a legal interest in property which has been ordered forfeited to the United States pursuant to this section may, within thirty days of the final publication of notice or his receipt of notice under paragraph (1), whichever is earlier, petition the court for a hearing to adjudicate the validity of his alleged interest in the property. The hearing shall be held before the court alone, without a jury.

(3) The petition shall be signed by the petitioner under penalty of perjury and shall set forth the nature and extent of the petitioner's right, title, or interest in the property, the time and circumstances of the petitioner's acquisition of the right, title, or interest in the property, any additional facts supporting the petitioner's claim, and the relief sought.

(4) The hearing on the petition shall, to the extent practicable and consistent with the interests of justice, be held within thirty days of the filing of the petition. The court may

consolidate the hearing on the petition with a hearing on any other petition filed by a person other than the defendant under this subsection.

(5) At the hearing, the petitioner may testify and present evidence and witnesses on his own behalf, and cross-examine witnesses who appear at the hearing. The United States may present evidence and witnesses in rebuttal and in defense of its claim to the property and cross-examine witnesses who appear at the hearing. In addition to testimony and evidence presented at the hearing, the court shall consider the relevant portions of the record of the criminal case which resulted in the order of forfeiture.

(6) If, after the hearing, the court determines that the petitioner has established by a preponderance of the evidence that—

> (A) the petitioner has a legal right, title, or interest in the property, and such right, title, or interest renders the order of forfeiture invalid in whole or in part because the right, title, or interest was vested in the petitioner rather than the defendant or was superior to any right, title, or interest of the defendant at the time of the commission of the acts which gave rise to the forfeiture of the property under this section; or
>
> (B) the petitioner is a bona fide purchaser for value of the right, title, or interest in the property and was at the time of purchase reasonably without cause to believe that the property was subject to forfeiture under this section;

the court shall amend the order of forfeiture in accordance with its determination.

(7) Following the court's disposition of all petitions filed under this subsection, or if no such petitions are filed following the expiration of the period provided in paragraph (2) for the filing of such petitions, the United States shall have clear title to property that is the subject of the order of forfeiture

and may warrant good title to any subsequent purchaser of transferee.

(m) If any of the property described in subsection (a), as a result of any act or omission of the defendant—

(1) cannot be located upon the exercise of due diligence;

(2) has been transferred or sold to, or deposited with, a third party;

(3) has been placed beyond the jurisdiction of the court;

(4) has been substantially diminished in value; or

(5) has been commingled with othe property which cannot be divided without difficulty;

the court shall order the forfeiture of any other property of the defendant up to the value of any property described in paragraphs (1) through (5).

§ 1964. Civil remedies

(a) The district courts of the United States shall have jurisdiction to prevent and restrain violations of section 1962 of this chapter by issuing appropriate orders, including, but not limited to: ordering any person to divest himself of any interest, direct or indirect, in any enterprise; imposing reasonable restrictions on the future activities or investments of any person, including, but not limited to, prohibiting any person from engaging in the same type of endeavor as the enterprise engaged in, the activities of which affect interstate or foreign activities of which affect interstate of foreign commerce; or ordering dissolution or reorganization of any enterprise, making due provision for the rights of innocent persons.

(b) The Attorney General may institute proceedings under this section. Pending final determination thereof, the court may at any time enter such restraining orders or prohibitions, or take such other actions, including the acceptance of satisfactory performance bonds, as it shall deem proper.

(c) Any person injured in his business or property by reason of a violation of section 1962 of this chapter may sue therefor in any appropriate United States district court and shall recover threefold the damaged he sustains and the cost of the suit, including a reasonable attorney's fee.

(d) A final judgment or decree rendered in favor of the United States in any criminal proceeding brought by the United States under this chapter shall estop the defendant from denying the essential allegations of the criminal offense in any subsequent civil proceeding brought by the United States.

§ 1965. Venue and process

(a) Any civil action or proceeding under this chapter against any person may be instituted in the district court of the United States for any district in which such person resides, is found, has an agent, or transacts his affairs.

(b) In any action under section 1964 of this chapter in any district court of the United States in which its shown that the ends of justice require that other parties residing in any other district be brought before the court, the court may cause such parties to be summoned, any process for that purpose may be served in any judicial district of the United States by the marshal thereof.

(c) In any civil or criminal action or proceeding instituted by the United States under this chapter in the district court of the United States for any judicial district, subpenas issued by such court to compel the attendance of witnesses may be served in any other judicial district, except that in any civil action or proceeding no such subpena shall be issued for service upon any individual who resides in another district at a place more than one hundred miles from the place at which such court is held without approval given by a judge of such court upon a showing of good cause.

(d) All other process in any action or proceeding under this chapter may be served on any person in any judicial dis-

trict in which such person resides, is found, has an agent, or transacts his affairs.

§ 1966. Expedition of actions

In any civil action instituted under this chapter by the United States in any district court of the United States, the Attorney General may file with the clerk of such court a certificate stating that in his opinion the case is of general public importance. A copy of that certificate shall be furnished immediately by such clerk to the chief judge or in his absence to the presiding district judge of the district in which such action is pending. Upon receipt of such copy, such judge shall designate immediately a judge of that district to hear and determine action.

§ 1967. Evidence

In any proceeding ancillary to or in any civil action instituted by the United States under this chapter the proceedings may be open or closed to the public at the discretion of the court after consideration of the rights of affected persons.

§ 1968. Civil investigative demand

(a) Whenever the Attorney General has reason to believe that any person or enterprise may be in possession, custody, or control of any documentary materials relevant to a racketeering investigation, he may, prior to the institution of a civil or criminal proceeding thereon, issue in writing, and cause to be served upon such person, a civil investigative demand requiring such person to produce such material for examination.

(b) Each such demand shall—

(1) state the nature of the conduct constituting the alleged racketeering violation which is under investigation and the provision of law applicable thereto;

(2) describe the class or classes of documentary material produced thereunder with such definiteness

and certainty as to permit such material to be fairly identified;

(3) state that the demand is returnable forthwith or prescribe a return date which will provide a reasonable period of time within which the material so demanded may be assembled and made available for inspection and copying or reproduction; and

(4) identify the custodian to whom such material shall be made available.

(c) No such demand shall—

(1) contain any requirement which would be held to be unreasonable if contained in a subpena duces tecum issued by a court of the United States in aid of a grand jury investigation of such alleged racketeering violation; or

(2) require the production of any documentary evidence which would be privileged from disclosure if demanded by a subpena duces tecum issued by a court of the United States in aid of a grand jury investigation of such alleged racketeering violation.

(d) Service of any such demand or any petition filed under this section may be made upon a person by—

(1) delivering a duly executed copy thereof to any partner, executive officer, managing agent, or general agent thereof, or to any agent thereof authorized by appointment or by law to receive service of process on behalf of such person, or upon any individual person;

(2) delivering a duly executed copy thereof to the principal office or place of business of the person to be served; or

(3) depositing such copy in the United States mail, by registered or certified mail duly addressed to such person at its principal office or place of business.

(e) A verified return by the individual serving any such demand or petition setting forth the manner of such service shall be prima facie proof of such service. In the case of ser-

vice by registered or certified mail, such return shall be accompanied by the return post office receipt of delivery of such demand.

(f)(1) The Attorney General shall designate a racketeering investigator to serve as racketeer document custodian, and such additional racketeering investigators as he shall determine from time to time to be necessary to serve as deputies to such officer.

(2) Any person upon whom any demand issued under this section has been duly served shall make such material available for inspection and copying or reproduction to the custodian designated therein at the principal place of business of such person, or at such other place as such custodian and such person thereafter may agree and prescribe in writing or as the court may direct, pursuant to this section on the return date specified in such demand, or on such later date as such custodian may prescribe in writing. Such person may upon written agreement between such person and the custodian substitute for copies of all or any part of such material originals thereof.

(3) The custodian to whom any documentary material is so delivered shall take physical possession thereof, and shall be responsible for the use made thereof and for the return thereof pursuant to this chapter. The custodian may cause the preparation of such copies of such documentary material as may be required for official use under regulations which shall be promulgated by the Attorney General. While in the possession of the custodian, no material so produced shall be available for examination, without the consent of the person who produced such material, by any individual other than the Attorney General. Under such reasonable terms and conditions as the Attorney General shall prescribe, documentary material while in the possession of the custodian shall be available for examination by the person who produced such material or any duly authorized representatives of such person.

(4) Whenever any attorney has been designated to appear on behalf of the United States before any court or grand jury in any case or proceeding involving any alleged violation of this chapter, the custodian may deliver to such attorney such documentary material in the possession of the custodian as such attorney determines to be required for use in the presentation of such case or proceeding on behalf of the United States. Upon the conclusion of any such case or proceeding, such attorney shall return to the custodian any documentary material so withdrawn which has not passed into the control of such court or grand jury through the introduction thereof into the record of such case or proceeding.

(5) Upon the completion of—

(i) the racketeering investigation for which any documentary material was produced under this chapter, and

(ii) any case or proceeding arising from such investigation, the custodian shall return to the person who produced such material all such material other than copies thereof made by the Attorney General pursuant to this subsection which has not passed into the control of any court or grand jury through the introduction thereof into the record of such case or proceeding.

(6) When any documentary material has been produced by any person under this section for use in any racketeering investigation, and no such case or proceeding arising therefrom has been instituted within a reasonable time after completion of the examination and analysis of all evidence assembled in the course of such investigation, such person shall be entitled, upon written demand made upon the Attorney General, to the return of all documentary material other than copies thereof made pursuant to this subsection so produced by such person.

(7) In the event of the death, disability, or separation from service of the custodian of any documentary material produced under any demand issued under this section or the

official relief of such custodian from responsibility for the custody and control of such material, the Attorney General shall promptly—

(i) designate another racketeering investigator to serve as custodian thereof, and

(ii) transmit notice in writing to the person who produced such material as to the identity and address of the successor so designated.

Any successor so designated shall have with regard to such materials all duties and responsibilities imposed by this section upon his predecessor in office with regard thereto, except that he shall not be held responsible for any default or dereliction which occurred before his designation as custodian.

(g) Whenever any person fails to comply with any civil investigative demand duly served upon him under this section or whenever satisfactory copying or reproduction of any such material cannot be done and such person refuses to surrender such material, the Attorney General may file, in the district court of the United States for any judicial district in which such person resides, is found, or transacts business, and serve upon such person a petition for any order of such court for the enforcement of this section, except that if such person transacts business in more than one such district such petition shall be filed in the district in which such person maintains his principal place of business, or in such other district in which such person transacts business as may be agreed upon by the parties to such petition.

(h) Within twenty days after the service of any such demand upon any person, or at any time before the return date specified in the demand, whichever period is shorter, such person may file, in the district court of the United States for the judicial district within which such person resides, is found, or transacts business, and serve upon such custodian a petition for an order of such court modifying or setting aside such demand. The time allowed for compliance with the demand in whole or in part as deemed proper and

ordered by the court shall not run during the pendency of such petition in the court. Such petition shall specify each ground upon which the petitioner relies in seeking such relief, and may be based upon any failure of such demand to comply with the provisions of this section or upon any constitutional or other legal right or privilege of such person.

(i) At any time during which any custodian is in custody or control of any documentary material delivered by any person in compliance with any such demand, such person may file, in the district court of the United States for the judicial district within which the office of such custodian is situated, and serve upon such custodian a petition for an order of such court requiring the performance by such custodian of any duty imposed upon him by this section.

(j) Whenever any petition is filed in any district court of the United States under this section, such court shall have jurisdiction to hear and determine the matter so presented, and to enter such order or orders as may be required to carry into effect the provisions of this section.

(2)

No. 91-641

IN THE

Supreme Court of the United States

OCTOBER TERM, 1991

RICHARD A. FENN, JAMAL RADWAN, SAUDI EUROPEAN INVESTMENT CORPORATION N.V., ALEF INVESTMENT CORPORATION N.V., and ALEF BANK, S.A.,

Petitioners,

vs.

ABDULAZIZ A. ALFADDA, ABDULLAH ABBAR, ABDULLA KANOO, ABDULAZIZ KANOO, YUSIF BIN AHMED KANOO (a Partnership Company), and AHMED A. ZAINY,

Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

RESPONDENTS' BRIEF IN OPPOSITION

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QUESTION PRESENTED

If foreign investors are defrauded by Americans acting through a New York-domiciled enterprise, may these investors seek relief under the civil RICO statute where:

(1) They were induced to purchase shares in a Netherlands Antilles holding company and told that proceeds from the stock offering would be used to fund a U.S. investment program;

(2) The fraud was accomplished by U.S. citizens acting through federally and New York-licensed banking agencies, who engaged in the substantial and systematic use of the U.S. wires and mails and the transportation of fraudulently obtained money and securities in interstate and foreign commerce; and

(3) The fraud was consummated when the enterprise (a) oversubscribed the stock offering through sales made in the U.S., (b) diverted offering proceeds within the U.S. to purchase a U.S. company for the benefit of some of the enterprise's more favored shareholders, and (c) enlisted the assistance of a U.S. company and its executives to conceal this fraud.

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No. 91-641

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Plaintiffs-Respondents Abdulaziz A. Alfadda, Abdullah Abbar, Abdulla Kanoo, Abdulaziz Kanoo, Yusif Bin Ahmed Kanoo (a Partnership Company), and Ahmed A. Zainy (hereinafter collectively "the Respondents") submit this brief in opposition to the petition of Defendants-Petitioners Saudi European Investment Corporation N.V. ("SEIC"), Alef Investment Corporation N.V., Alef Bank, S.A., Richard A. Fenn, and Jamal Radwan (hereinafter collectively "the Petitioners") for a writ of certiorari to review the judgment of the United States Court of Appeals for the Second Circuit, entered in this case on June 5, 1991. That judgment reversed the decision of the United States District Court for the Southern District of New York dismissing the amended complaint for lack of federal subject matter jurisdiction.

STATEMENT OF THE CASE

Through omission and distortion, Petitioners have reshaped the record below and the conclusions of the Second Circuit almost beyond recognition. Petitioners present this case as one involving a "wholly foreign transaction" bearing only a "peripheral" and "incidental" relationship to the United States. They are able to characterize the conduct at issue as "wholly foreign" only by ignoring the substantial, jurisdictionally relevant activity that took place in the United States, or by conclusorily labeling that activity "peripheral." They overcome other facts unfavorable to their theory of the case by misstating those facts. They condemn the Second Circuit for not applying a "conduct or effects" analysis, even though the court plainly applied that very test in sustaining subject matter jurisdiction under both the federal securities laws and RICO.

In fact, this case does not involve the "extraterritorial" application of any statute, since most of the conduct complained of occurred in the United States. Rather, this case presents the question of whether the courts of the United States may exercise jurisdiction over an action brought by the foreign victims of a transnational securities fraud that was engineered and consummated in the United States by United States citizens and their corporate affiliates, including two New York-licensed banks. These banks and the individuals responsible for their management first solicited Respondents to help capitalize their U.S. investment plan, then defrauded Respondents through a pattern of illicit activities carried out in New York and elsewhere in the United States. They prepared a fraudulent stock prospectus here and arranged to have it distributed to foreign investors, allegedly from Paris. They then proceeded to dilute Respondents' shareholdings by selling excessive voting shares in the United States. They diverted the proceeds of the fraudulent stock offering to United States investments for the purpose of benefitting themselves and certain favored investors. Lastly, they conspired with one U.S. investor (Charles Keating) not to divulge the fraud to other investors and engaged in additional, substantial activities in the United States that were designed to cover up their fraud. These acts within the United States were integral, not peripheral, to the Petitioners' consummation of the fraudulent scheme. These acts directly caused the losses suffered by Respondents.

Petitioners contend that in sustaining federal jurisdiction under RICO, the Second Circuit should have but did not apply the "conduct or effects" test to determine whether a U.S. statute may be applied to international transactions. Petitioners misread the decision below. The Second Circuit expressly applied the test Petitioners say it did not, to jurisdictionally determinative facts Petitioners belittle but cannot deny. After doing so, the court properly concluded that federal jurisdiction exists under both the federal securities laws and RICO.

This case neither breaks new ground, extends the jurisdictional reach of RICO, nor conflicts with the decisional law of other circuits or of this Court. Where, as here, American citizens mobilize capital for the express purpose of U.S. investment, bring the investment proceeds to New York and then divert the funds here, those responsible should reasonably expect to be subject to this country's laws and judicial process.

As a matter of fact, law, and policy, the decision of the Second Circuit is correct, and no basis exists for the grant of certiorari.

A. The Parties[1]

Plaintiffs-Respondents Alfadda, Zainy, Abbar, and the Kanoos are residents and citizens of Saudi Arabia and Bahrain. Each owns voting stock in Defendant-Petitioner SEIC.

All of the key participants in the fraudulent scheme are United States citizens. Petitioner Jamal Radwan, the Chairman of SEIC, is a U.S. citizen who spends much of his time in New York. (E-392.)[2] Petitioner Richard Fenn, the former Vice-Chairman of

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[1] On Petitioners' motion to dismiss and the subsequent appeal, the largely undisputed facts alleged in the amended complaint are deemed to be true. Wright and Miller, Federal Practice and Procedure § 1350 at 220 (2d ed. 1990). To the extent, if any, that the court of appeals disagreed with the district court's "factual findings," it was free to take its own view of the facts established through a purely documentary record. *Taylor v. Lombard*, 606 F.2d 371, 372 (2d Cir. 1979), *cert. denied*, 445 U.S. 946 (1980).

[2] References to "A____" and "E____" are to pages of the Joint Appendix and Exhibits, respectively, filed in the Court of Appeals.

SEIC, is a U.S. citizen who resided in New York City during the period at issue and who now resides in Pawling, New York. (E-336.) Radwan and Fenn enlisted two other U.S. citizens to help structure and market the SEIC offering: Mario Diaz-Cruz (a New York lawyer who served as SEIC's general counsel) and Ronald Reilly (the president of Capital International, Inc. ("Capital"), a Texas corporation hired by SEIC to develop and market the offering).[3] Currently, Diaz-Cruz lives in New York and Reilly lives in Connecticut. (A-2 Nos. 23, 24; A-124; A-125.)

During the period relevant to this litigation (*i.e.*, from 1983 to the filing of the original complaint), all corporate Defendants-Petitioners either (a) were licensed federally or by the State of New York as foreign banking organizations, or (b) regularly conducted U.S. business through establishments here. Collectively these corporate defendants refer to themselves as the "Saudi European Group." (E-257; E-360-62.)

The parent company of the Saudi European Group was Petitioner SEIC, a closely-held Netherlands Antilles company. SEIC was formed in 1979 to develop investment opportunities in "western markets" for its shareholders and clients. (E-185.) During the relevant period, SEIC conducted substantial business activities in the U.S. from offices at Rockefeller Plaza in New York City.[4] (E-112-13; E-260-61; E-264; E-282-92; E-316-34.)

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[3] Although Diaz-Cruz and Reilly were not named as defendants in this action, they were sued by Resolution Trust Corporation in a related case in the Southern District of New York involving the same SEIC securities offering, captioned *Resolution Trust Corporation, as Conservator of Lincoln Federal Savings & Loan Association, et al. v. Richard A. Fenn, et al.*, C.A. No. 90-Civ-6050. The Resolution Trust case has been transferred by the Judicial Panel on Multidistrict Litigation for pretrial discovery in connection with other related litigation against SEIC, Fenn and SE Bank in the District of Arizona, captioned *In re American Continental Corp./Lincoln Savings and Loan Securities Litigation*, MDL Dock No. 834.

[4] SEIC's registered office was in Curacao at the headquarters of Pierson Trust (Curacao) N.V. (E-45; E-393.) However, SEIC did business through the U.S. mails and wires at the office of its subsidiaries and affiliates, including the New York City offices of the Saudi European Group and SE Bank. (E-197; E-378-79 at ¶¶ 2, 3.)

SEIC's most significant subsidiary was the Saudi European Bank ("SE Bank"). During the period relevant to this litigation, SE Bank maintained offices in New York City at Rockefeller Center, as well as in Paris and in Bahrain. (E-1-3; E-281; E-283.) The New York State Banking Department licensed the New York office as a "representative" bank in 1981 and upgraded the office to "agency" status in 1985. (E-338; E-254-55.) SEIC and SE Bank were both U.S. dollar-based foreign banking organizations licensed by the Federal Reserve Board. In their 1985 financial report to the Federal Reserve, SEIC and SE Bank reported U.S. banking assets of $166,000,000. (E-285.)

Defendants-Petitioners Radwan and Fenn managed SEIC and its affiliates during the relevant period. Both individuals held positions as "principal officers" of Petitioner Alef Investment Corporation N.V. ("Alef"), an offshore holding and management services company. The management of SEIC was contracted to Alef (E-8-18; E-53), under an agreement providing that all SEIC employees are employees of Alef. SEIC, in turn, owned 15% of Alef. (E-19-20.)

Alef owned Petitioner Alef Bank, S.A. ("Alef Bank") through a Dutch intermediary corporation. (E-19.) In 1983, Alef Bank applied to the New York Banking Department to operate a "representative office" in the same suite as SE Bank. (E-4.) In July of 1984, Alef Bank was issued a license to operate such an office under the direction of Petitioner Fenn. (E-5-6; E-145.) Both Alef and Alef Bank were underwriters of the stock offering at issue (E-44; E-638 at ¶ 9), in which capacity these companies presumably earned the $1 million in discounts and fees disclosed in the Prospectus. (E-49.)

B. The Fraudulent Scheme

1. Preparation Of The Fraudulent Prospectus In The United States

During 1983 and 1984, SEIC's Chairman Radwan and Vice Chairman Fenn devised a scheme to raise substantial capital from investors – ostensibly for legitimate use by SEIC as part of its U.S. investment program – with the ultimate goal of creating

"a public energy company quoted on the U.S. stock exchanges." (E-52.) One of the key steps in this plan was the drafting and preparation of a placement memorandum for distribution to potential investors ("the Prospectus"). (E-44-57.) This document was drafted and prepared in the United States.

To effectuate the U.S. investment program, Petitioners Radwan and Fenn met with Reilly in Atlantic City in September of 1983. (E-22-24; E-357-58.) As a result of these meetings, SEIC retained Reilly's Texas-based company, Capital International, Inc., to prepare the Prospectus and assist SEIC in launching the U.S. investment program. (E-25-30; E-356.) SEIC's contract with Capital provided a bonus for Capital's successful marketing of SEIC's offering in the U.S. and elsewhere. (E-30.)

During October of 1983, SEIC's Texas-based agent, Reilly, drafted portions of the Prospectus in Houston. (E-58; E-363-64; E-885-86.) At the same time, SEIC's general counsel (New York lawyer Diaz-Cruz) worked with Radwan to arrive at the appropriate capitalization formula. (E-32-39.) On November 23, 1983, Reilly telexed Radwan from Houston suggesting that Reilly would "complete production of prospecti in Houston" and review the document with SEIC's general counsel in New York the following week. (E-40.) As planned, Reilly completed production of the Prospectus through the "galley proof" stage in Houston and edited the galley proofs with Diaz-Cruz in New York during the first week of December, 1983. (E-41; E-368-72; E-637 at ¶ 7.) According to Reilly, the Prospectus itself was subsequently printed in Paris as a cost-saving measure. (E-841.) Throughout the latter part of 1983, Diaz-Cruz continued to develop the details of the offering with Radwan and Reilly through a series of telexes and memoranda sent to, from and within the U.S. (E-32-38.)

2. The Purpose Of The Offering: SEIC's U.S. Investment Program

The Prospectus clearly sets forth SEIC's investment objectives. These objectives were to be centered in the United States and included:

(1) investment in U.S. financial institutions, one in Texas, the other in Florida (E-48; E-52);

(2) expansion of SEIC's marketable securities in the energy sector, with the ultimate objective being "to assemble, develop and spin-off the acquired assets into a public energy company quoted on the U.S. stock exchanges" (E-48; E-52);

(3) expansion of merchant banking activities, including the opening of an office in New York (E-48); and

(4) expansion of the operations of SE Bank, which already maintained an office in New York managed by Fenn (E-48).

In October of 1983, Diaz-Cruz confirmed in a telephone conversation with Radwan that "[t]he additional capital of SEIC. . .will be used for investments in the United States. . . ." (E-34.)

3. SEIC's Disclosed Capital Structure

SEIC was initially capitalized through the 1979 sale of 20,000 shares, marketed at a price of $1,000 per share. Another 20,000 shares of SEIC voting stock was authorized but remained unissued. In 1979, plaintiff Alfadda paid $1 million to acquire 1,000 shares of SEIC voting stock in this initial offering, based partly upon assurances that he would thereafter enjoy a preference to participate proportionately in future SEIC share issuances. (E-420.)

Through the offering described in the 1984 Prospectus, Petitioners sought to increase SEIC's capital by approximately $60 million. This was to be accomplished through a complex capitalization formula designed to leave SEIC with a total capital base of 1.2 million voting shares at the conclusion of a fully subscribed offering. (E-43; E-457.) Based on this capitalization formula, 600,000 voting shares ("Class A Shares") were to be sold in the 1984 offering. The Prospectus reflected this capitalization formula and represented that any oversubscriptions were to be allocated to up to 1,800,000 *non-voting* certificates ("Class AA shares") on a proportionate basis. (E-47; E-57.)

4. Petitioners' Misrepresentations

The Prospectus contained several material misrepresentations. First, the Petitioners represented that non-voting certificates would be issued in the event of an oversubscription. This clearly was intended to assure investors that no dilution of their voting shares would occur. The Prospectus also provided that existing shareholders of SEIC, such as Alfadda, would be given the first opportunity to participate in the offering. (E-47.) To the extent voting shares were not bought by the existing shareholders, the Prospectus represented that new investors could acquire the remainder of the 600,000. Finally, the Prospectus specifically represented that investors would enjoy preemptive rights to participate, on a pro rata basis, in any additional offerings or issuances of SEIC stock. (E-57.)[5]

5. Respondents' Detrimental Reliance Upon The Petitioners' Misrepresentations

In April of 1984, Respondents Abbar, Zainy and the Kanoos each purchased 10,000 shares of SEIC stock for $1 million, respectively. In making these purchases, Respondents relied upon the representations contained in the Prospectus. Respondents concede they received the Prospectus in the Middle East. Although Respondent Alfadda, as a founding shareholder of SEIC, possessed preemptive rights at the time of the 1984 SEIC offering, he was never given a copy of the Prospectus nor afforded any opportunity to participate in the 1984 offering.

6. Petitioners' Deposit Of Investment Funds In United States Bank Accounts

Defendants-Petitioners arranged to have the proceeds from the Offering transferred to New York escrow accounts. On April 9, 1984, the Kanoos authorized the transfer of $1 million to the account of SE Bank's Bahrain branch at Chemical Bank in New York (E-61), which transfer was confirmed by Chemical Bank

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[5] The Prospectus contained an additional statement indicating that SEIC's capital base included approximately $20 million of subordinated "capital notes." (E-56.) The Prospectus did not disclose, however, that these "capital notes" could be converted into voting stock, nor that Petitioner Radwan had taken steps to convert the "capital notes" into an additional 600,000 voting shares. (E-383.) This lack of full disclosure constituted a material omission.

telex dated April 13, 1984. (E-725.) Before SEIC closed the Offering, SE Bank transferred the $1 million paid by the Kanoos (together with $10 million in offering proceeds from other investors) to the escrow account that SEIC had established at European American Bank in New York City.[6] (E-72.) This escrow account was similarly the final resting place for the $1 million that Respondents Zainy and Abbar paid, respectively, to receive 10,000 shares of SEIC. (A-140; E-45; E-67; E-71; E-119.)

7. The Dilution Through Sales In The United States

Petitioners' version of the relevant facts ends abruptly in April 1984, with each Respondent's remittance of $1 million for the purchase of 10,000 shares of SEIC stock. The scheme to defraud Respondents entailed far more.

By the end of May 1984, SEIC had obtained subscriptions for approximately 345,500 of the 600,000 voting shares described in the Prospectus. (E-132-34.) Although the closing had originally been set for March 31, 1984, it was postponed on several occasions, thereby permitting the further sale of SEIC voting shares in the U.S. market. (E-47; E-67; E-87; E-119; E-123.) Closing did not in fact occur until October 1984. (E-210-216.) During the period April-June of 1984, Fenn and Radwan (together with Reilly) negotiated sales of 330,000 additional voting shares. These sales were made in the U.S. to American Continental Corporation ("ACC") and Mr. Abdulrahman Al-Turki, a Saudi Arabian businessman then working in Houston. Not only did the sales occur in the United States, but substantial activity took place in the U.S. in connection with their negotiation and confirmation.[7] By virtue of these two U.S. sales, SEIC fraudulently diluted the interests of SEIC's investors, including Respondents'.

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[6] Although Petitioners deny that the EAB account was an "escrow" account, Reilly himself referred to it as the "escrow deposit account." (E-71.) His terminology was apt. "Escrow" is defined in *Webster's New Collegiate Dictionary* at 390 (1976 ed.) as "money. . .delivered to a third person to be delivered by him to the grantee only upon the fulfillment of a condition." Here the condition was the delivery of the SEIC bearer shares upon closing.

[7] On April 15, 1984, Fenn met Charles Keating, Chairman of ACC, in New York City and advised Keating of the SEIC offering. (E-66; E-340-46.) Soon

(Footnote continued)

8. The Closing In The United States

The closing of the SEIC Offering (*i.e.*, the exchange of investor funds in escrow for the stock certificates) did not take place until at least October 12, 1984 — the date share certificates were issued to Respondents Abbar, Zainy and Kanoos. (E-210-15.) Some purchasers did not receive their share certificates until later. (E-216-19.)

As part of the closing, SEIC designated a New York bank account as the final resting place for investors' funds. (E-45; E-67; E-71; E-119.) Investor funds collected at SE Bank branches in Bahrain and Paris were transferred to a New York office of European American Bank in anticipation of the New York closing (E-67; E-72-73), which could not occur until all shareholder funds were collected in New York. (E-67; E-119.) At least $45 million in proceeds from the Offering was transferred to accounts maintained for SEIC in New York City. (E-72-73; E-102-04; E-466-68.)

9. Exportation Of Stock Certificates From The United States

At any point up until the Petitioners transferred the stock certificates from the U.S., they could have remedied the fraudulent

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thereafter, Fenn informed Radwan that Keating "would like to take a stake in our [SEIC's] capital offering." (*Id.*) In early May, 1984, ACC sent a letter from Phoenix to Reilly advising him that ACC's savings and loan subsidiary desired to acquire a 15% interest in SEIC. (E-68.) Upon receipt of ACC's letter, Reilly telexed SEIC's auditor to inform him that ACC, "a major (15%) new shareholder of SEIC," required "assistance in setting up an offshore company to hold its investment." (E-69.) Before ACC's offshore shell existed, SEIC telexed ACC in Phoenix to advise that it had accepted ACC's offer to purchase 15% of SEIC (180,000 shares) for $18 million and directed ACC to deposit the money in a New York bank account. (E-71.) In response, on June 1, 1984, Lincoln Savings and Loan Association, an ACC subsidiary, transferred $18 million in "federal funds" to a New York bank account. (E-102-04.)

SEIC also diluted plaintiffs' interests in June of 1984 by selling 150,000 shares of stock to Mr. Al-Turki in Houston. Reilly clearly considered the sale to Al-Turki to be a domestic sale because he telexed Radwan from Houston advising that any sale to Al-Turki should result in Reilly's earning a bonus for a U.S. sale under the bonus provision in the Capital contract. (E-59.) On June 26, 1984, Reilly telexed Al-Turki in Houston accepting Al-Turki's June 22 offer and instructing him to send his funds to Manufacturers Hanover Bank in New York. (E-126; *see also* E-116; E-120; E-124.)

dilution caused by their oversubscription of voting shares. During July and August of 1984, Radwan, Fenn, Diaz-Cruz and Reilly were aware that only voting stock had been sold under the SEIC Offering. Accordingly, they must have known that subscribers' interests were being improperly diluted. (E-142.) In August 1984, Diaz-Cruz drafted the text of the SEIC voting stock certificates, communicated their content to Radwan in Paris, and arranged for the shares to be printed in New York. (E-148-52; E-181; E-199; E-202.) At Radwan's direction (E-199), Diaz-Cruz had 2,000 share certificates (representing well over 1.2 million voting shares) printed in New York. (E-202; E-210-15.) On September 27, 1984, the day before the engraver delivered the printed shares to Diaz-Cruz, Radwan and Fenn met with Charles Keating in Washington, D.C. and explained the "dilution aspects" of the Offering to him. (E-208-09; E-297-98.)

During the first week of October 1984, Radwan and Diaz-Cruz met in New York to assign the shares to subscribers. (E-538.) After making the assignments, share certificates representing almost 2 million voting shares were sent to Europe. (*Id.*) At that time, Radwan, Fenn, Diaz-Cruz and Reilly knew that the Offering was oversubscribed and that the issuance would result in a dilution. (E-120-21; E-142; E-164-68; E-178-80; E-297-303.) Respondents received those documents on or around October 12, 1984. (E-210-11; E-212-13; E-214-15.)

10. The Diversion Of Proceeds In The United States

Plaintiffs-Respondents alleged that proceeds obtained from the SEIC offering were diverted in the U.S. and used to benefit SEIC's management and certain favored shareholders. (A-152-54.) In particular, Respondents challenged the purchase of a U.S. enterprise, Gulf Oil Trading Corp. ("GOTCO"), immediately after the close of the SEIC Offering.

Consistent with SEIC's stated objectives, Reilly searched during August 1984 for a "cornerstone energy investment," which was to become a publicly-traded U.S. energy company. (E-112.) Radwan recommended the Houston-based energy company, GOTCO. (E-146-47.) Over Reilly's objection (E-201), Petitioners apparently arranged for GOTCO to be purchased not for the

benefit of SEIC, but for the benefit of certain favored SEIC shareholders. This is reflected in the Saudi European Group's 1985 Annual Report, where it states that in November of 1984, "some [Saudi European] Group shareholders purchased GOTCO [Gulf Trading Company] from Chevron." (E-261.)

The amended complaint alleges a further diversion of proceeds, consisting of the purchase of convertible preferred stock in Galveston-Houston Company, a Houston company traded on the New York Stock Exchange.[8] (A-154-55.)

11. The Cover-Up In The United States

Having fraudulently diluted Respondents' interests, the Petitioners took steps in the U.S. to suppress the discovery of their fraud. In August 1984, ACC asked SEIC to confirm the existence of only 1.2 million voting shares and to clarify the conversion rights, if any, of the "capital notes." (E-155.) ACC's letter threatened to expose the oversubscription and the fraudulent conversion of SEIC's "capital notes." Reilly quickly forwarded ACC's inquiry to Radwan, Fenn and Diaz-Cruz (E-164), urging Radwan to review the matter promptly with Diaz-Cruz. (E-177.) As a result, Radwan instructed Fenn to arrange a meeting with Charles Keating to answer the charges made in ACC's letter. (E-183.)

On September 27, 1984, Radwan and Fenn met Keating in Washington D.C., and explained that the "legalese" raised by Keating's lawyers was inconsistent with the "family orientation" of SEIC. (E-208.) In Fenn's written account of the meeting, Fenn conceded the "dilution aspects" of the offering and indicated that SEIC was prepared to offer Keating additional shares to offset the dilution of ACC's interests. (*Id.*) Radwan reiterated this offer at a March 1985 meeting with Keating in Florida, during which Radwan offered to sell Keating a block of 80,000 to 130,000 shares to make up for the dilution. (E-224-26.)

In May 1985, ACC's general counsel insisted to Fenn that ACC owned 15%, despite Radwan's statement to Keating that ACC's

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[8] Because the district court barred plaintiffs from conducting discovery on the issue of diversion (A-89), this and additional examples of diversion of the Offering proceeds could not be pursued.

interest "got watered down somewhat to 10%." (E-223; E-304.) The complaints from ACC continued in 1986 (E-304), but were silenced in 1987, when Charles Keating and his group aided Petitioner Radwan in deflecting inquiries from other SEIC shareholders about SEIC's capital structure. (E-313-15.)[9]

C. The Decisions Below

1. The District Court

Plaintiffs-Respondents filed suit in the Southern District of New York, alleging violations of the Racketeer Influenced and Corrupt Organizations Act ("RICO"), 18 U.S.C. § 1961-68; section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b); Rule 10b-5 of the Securities and Exchange Commission, 17 C.F.R. § 240-10b-5; common law fraud; breach of fiduciary duty; and rescission of contract.[10] After permitting plaintiffs only limited discovery, the court granted defendants' motion to dismiss, holding that it lacked subject matter jurisdiction over the securities fraud and RICO claims. Accordingly, the court dismissed the pendent state claims as well.

Under the traditional tests applied by the district court, subject matter jurisdiction exists with respect to a foreign plaintiff's claim under the securities laws if the plaintiff meets either the "conduct" test or the "effects" test. Here, the district court saw the fraud as having been "committed by placing the allegedly fraudulent prospectus in the plaintiffs' hands." Since "plaintiffs received the prospectus outside the United States," the district court concluded that the fraud had an insufficient nexus with this country to sustain federal jurisdiction. (20a.)[11] Given the

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[9] In *Lincoln Savings and Loan Ass'n v. Wall*, 743 F. Supp. 901, 916 (D.D.C. 1990), Judge Sporkin found that Lincoln Savings and Loan engaged in a transaction with "an affiliate of the Saudi European Bank, an entity in which Lincoln held a 10% interest," which "was spurious from its inception." Judge Sporkin found that Lincoln and the SE Bank affiliate — *i.e.*, SEIC — had engaged in a "parking transaction" to misrepresent Lincoln's financial condition in 1987 and 1988.

[10] Respondent Alfadda did not join in the securities fraud claims, having acquired his interest in SEIC before 1984.

[11] References to "__ a" are to pages of the Appendix to the Petition for a Writ of Certiorari. References to "Pet. at __" are to pages of the Petition itself.

court's opinion that the fraud was complete upon plaintiffs' receipt of the Prospectus, it discounted as "peripheral" and of no jurisdictional relevance the subsequent U.S. activity resulting in the dilution of plaintiffs' stock and diversion of the proceeds, which, in plaintiffs' view, was an integral and culminating part of the continuing fraud.

The district court also dismissed the RICO claim (21a-27a.), holding that the standards for applying RICO to transnational transactions, "at least when RICO is asserted, as here, to recover for what at bottom is a securities fraud – should be consistent" with the standards for applying the securities laws. (23a-24a.) Since the court had already concluded there was no subject matter jurisdiction over the securities fraud claims, it held that RICO jurisdiction was lacking as well. The court reiterated its view that "[t]he principal activity complained of – the communication of fraudulent representations – took place outside of the United States, and the effects of that activity were felt by foreign nationals outside of the United States." (24a.) Characterizing as "subsidiary to the securities fraud" the numerous predicate acts and other U.S. activity relating to the sales to ACC and Al-Turki, the court held:

> [W]hen the RICO predicate acts occurring in the United States consist of subsidiary uses of United States communications and transportation systems, but the underlying fraud occurs outside the United States, the Court lacks subject matter jurisdiction over the RICO claim.

(25a.)

2. The Court of Appeals

The Second Circuit reversed, holding that federal jurisdiction exists under both the securities laws and RICO. Although it, like the district court, focused on the "conduct" test and dealt with the same basically undisputed facts, the circuit court differed fundamentally with the trial court's view of the critical elements of the fraud – especially the legal significance of the undisputed events that transpired in the United States after Respondents had received the Prospectus. (7a.)

As noted above, the district court deemed the fraud complete when Respondents received the Prospectus containing the misrepresentations, and dismissed as "peripheral" the subsequent sales of SEIC stock in the U.S. to ACC and Al-Turki. The court of appeals, on the other hand, drew from a long line of its own precedents holding that where conduct is carried out in the United States to *consummate* the alleged fraud, that conduct will be considered relevant for purposes of subject matter jurisdiction. The Second Circuit properly recognized that some of the misrepresentations in the Prospectus did not — indeed could not — become fraudulent until the subsequent U.S. sales actually diluted Respondents' shares: "[T]he prospectuses did not become fraudulent until additional voting shares were sold to Lincoln and Al-Turki." (8a.) The court held that the U.S. activity associated with these sales fully satisfied the traditional "conduct" test. (*Id.*) Thus, the court found subject matter jurisdiction over the Respondents' securities fraud claims.

Turning to the RICO claim, the court acknowledged that, as with the securities laws, RICO is silent concerning its application to transnational conduct. The court did, however, acknowledge this Court's repeated admonition that RICO is to be broadly rather than parochially construed. (10a.) Accordingly, the court held that the mere fact that the corporate defendants (and alleged RICO enterprises) were incorporated abroad did not "immunize them from the reach of RICO." (*Id.*) To determine whether Congress would have intended the court to exercise jurisdiction over Respondents' RICO claims, the court next proceeded (as in any federal case with some foreign elements) to examine whether the conduct being challenged under RICO was sufficient to satisfy the "conduct or effects" test.

Contrary to Petitioners' charge, the court of appeals did not ignore the test of "conduct or effects" in the United States and focus on isolated instances of mail and wire fraud. Rather, the court expressly incorporated by reference its earlier analysis under the securities laws. First, it acknowledged that "[a]mong the predicate acts alleged by plaintiffs are the securities fraud violations consummated by the sales of SEIC shares to Lincoln American Investments and Al-Turki." (10a.) Second, it explicitly

incorporated its prior "conduct or effects" analysis of those predicate acts:

> As discussed *supra*, we disagree with the district court's holding that the alleged fraud was complete upon delivery of the misrepresentations contained in the prospectuses and the subsequent purchases of SEIC stock by plaintiffs Abbar, Zainy and the Kanoos in April 1984. The sales to Lincoln American Investments and Al-Turki were predicate acts which occurred primarily in the United States, and hence, serve as a basis of subject matter jurisdiction for the RICO claims.

(10a-11a.) Thus, on the fully reasoned basis of its prior "conduct or effects" analysis, the Second Circuit found federal jurisdiction over Respondents' RICO claim, reversed the district court's dismissal, and remanded to the trial court for further proceedings.[11]

SUMMARY OF ARGUMENT

1. Petitioners completely misread the Second Circuit's decision when they argue that the court of appeals failed to apply the "conducts or effects" test in determining jurisdiction under RICO. The court conducted just such an analysis earlier in its opinion, when it addressed jurisdiction over Respondents' securities fraud claims and concluded that jurisdiction existed over those claims under the "conduct" test. When it turned to address jurisdiction under RICO, the Second Circuit noted that the earlier discussed securities fraud claims also constitute predicate acts under RICO. It therefore expressly incorporated by reference its earlier analysis and held that the U.S. conduct that was sufficient to support jurisdiction over the securities fraud claims was, for the same reasons, sufficient to support RICO jurisdiction.

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[11] Petitioners seek review in this Court only of the Second Circuit's ruling on RICO jurisdiction, claiming that the "securities claims are time-barred under this Court's recent decision in *Lampf, Pleva, Lipkind, Prupis & Petigrow v. Gilbertson*, 111 S. Ct. 2773 (1991). . . ." (Pet. at 4 n.3.) Defendants' motion raising that question is currently pending before the district court (as is their motion to dismiss for *forum non conveniens*), and Respondents in no way concede that their securities claims are time-barred.

2. The Second Circuit applied the "conduct or effects" test correctly. The record provides overwhelming evidence of conduct within the United States that effectuated and consummated Petitioners' fraudulent scheme and that directly caused the losses sustained by Respondents. This conduct within the United States is sufficient to sustain jurisdiction over Respondents' RICO claims. Moreover, Respondents' allege specific U.S. conduct by Petitioners that establishes jurisdictionally sufficient predicate acts in addition to securities fraud. These include mail fraud, wire fraud, and the illegal transportation of money and securities in interstate and foreign commerce.

3. The exercise of jurisdiction over Respondents' RICO claims is "reasonable" under the eight factors set forth in the Restatement (Third) of Foreign Relations.

4. The Second Circuit's decision is consistent with the law of all the other circuits and of this Court. U.S. citizens who conduct their activities here and use the instrumentalities of this country to defraud foreign investors cannot reasonably expect to evade the reach of the RICO statute. This is especially so in light of the courts' persistent and emphatic exhortations that RICO must be liberally and broadly construed.

ARGUMENT

THE SECOND CIRCUIT CORRECTLY HELD THAT THE PETITIONERS' CONDUCT WITHIN THE UNITED STATES, WHICH INCLUDED CERTAIN STATUTORY PREDICATE ACTS, WAS SUFFICIENT TO SUSTAIN SUBJECT MATTER JURISDICTION UNDER RICO

A. The Second Circuit Did Apply The "Conduct Or Effects" Test To Determine Subject Matter Jurisdiction Under RICO

Petitioners contend that the Second Circuit "announc[ed] a new rule for the exercise of subject matter jurisdiction" under RICO (Pet. at 8), a rule based entirely on the "peripheral" and "incidental" use of United States mails and wires. (Pet. at 9.) They then compound their foray into fiction by asserting that the court "fell into this error by departing from the test of 'substantial conduct or effects in the United States'. . . ." (Pet. at 3.)

Petitioners are correct that courts have applied some variant of the "conduct or effects" test when examining subject matter jurisdiction under RICO in the context of international fraudulent schemes. *See, e.g., Republic of Philipines v. Marcos*, 862 F.2d 1355 (9th Cir. 1988) (*en banc*), *cert. denied*, 490 U.S. 1035 (1989) (conduct and effects test); *United States v. Noriega*, 746 F. Supp. 1506 (S.D. Fla. 1990) (effects test). Petitioners simply defy reality, however, when they suggest that the Second Circuit failed to apply that analysis in the instant case.

Respondents asserted two statutory bases for federal jurisdiction: the federal securities laws and RICO. The court addressed the former first, since the essence of the fraud at issue involves the dilution of a securities offering and the diversion of its proceeds. Acknowledging that the appropriate standard was the "conduct or effects" test, the Second Circuit devoted the bulk of its opinion to applying the "conduct" test to "plaintiffs' largely uncontested allegations" of activities that took place in the United States. (6a-7a.) Concluding that the conduct within the United States was integral to the fraudulent scheme and necessary to consummate the fraud, the court held that under the "conduct" test, the court had jurisdiction over the securities fraud claims.

The court then turned to the RICO claim. It began by observing that "among the predicate acts alleged" by Respondents were the securities fraud violations it had just finished reviewing. It then noted that the district court had dismissed the RICO claim for the same reason it had dismissed the securities fraud claims: its view that the fraud was complete upon receipt of the Prospectus. (10a.) Invoking its prior analysis, the court then said:

> As discussed *supra*, we disagree with the district court's holding. . . .The sales to Lincoln American Investments and Al-Turki were predicate acts which occurred primarily in the United States, and hence, serve as a basis of subject matter jurisdiction for the RICO claims.

(10a-11a.)

The incorporation by reference of its prior analysis could not be clearer. Having already analyzed the Petitioners' activities under the "conduct" test, there was no reason to repeat the exercise. The court reiterated the controlling facts. It then noted its disagreement with the lower court and repeated its reasons for having rejected that court's conclusion, thereby clearly incorporating the "conduct" analysis it had just performed in connection with the securities claims. It need do no more. Contrary to Petitioners' contention, the court clearly reached its conclusion on RICO jurisdiction by means of a "conduct or effects" analysis.

B. The Second Circuit Applied The "Conduct Or Effects" Test Correctly And Properly Concluded That Subject Matter Jurisdiction Exists Under RICO

Not only did the Second Circuit apply the analytical test Petitioners falsely say it ignored; the court applied that test correctly.

The court properly began its analysis by examining the text of the statute. Where, as here, the statute is silent as to its application to international transactions,[13] the next step is to examine Congressional intent. The Second Circuit did so, referring to its previously expressed conclusion that the statute "permits no inference that [it] was intended to have a parochial application." (10a, *quoting United States v. Parness*, 503 F.2d 430, 439 (2d Cir. 1974), *cert. denied*, 419 U.S. 1105 (1975)). This view is wholly consistent with the pronouncements of this Court, which has repeatedly rejected lower court attempts to erect arbitrary barriers to civil actions under RICO. *See, e.g., H.J., Inc. v. Northwestern Bell Tel. Co.*, 492 U.S. 229 (1989); *Sedima, S.P.R.L. v. Imrex Co.*, 473 U.S. 479 (1985). Finding no statutory impediment to the application of RICO to a case with international aspects, the court turned to an examination of the specific violations alleged here.

RICO catalogues numerous violations that can constitute the requisite predicate acts of "racketeering activity." 18 U.S.C.

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[13] RICO is not entirely silent with respect to its geographical scope. In describing every one of the prohibited activities, Congress referred to activities which "affect[] interstate *or foreign* commerce." 18 U.S.C. § 1962(a), (b), (c) (emphasis supplied). (36a-37a.)

§ 1961(1). (33a-34a.) Continually referring to "mails and wires," Petitioners would have this Court believe that the Second Circuit plucked a few isolated letters, telexes, and telephone calls from the record and relied upon these "attenuated" U.S. contacts to support RICO jurisdiction. Although Petitioners' violations of the mail and wire fraud statutes were indeed sufficient to sustain jurisdiction,[14] these violations were *not* the sole basis of the Second Circuit's decision.

Petitioners' ubiquitous mail and wire fraud offenses were part of a pattern of fraudulent conduct which included various devices. The statute expressly identifies fraud in the sale of securities as a predicate act. 18 U.S.C. § 1961(1)(D). (34a.) The Second Circuit based its "conduct or effects" analysis on Respondents' allegations of those violations, and specifically identified those violations as predicate acts under RICO.[15] (10a-11a.) The Second Circuit's analysis was correct.

1. The Test

The "conduct or effects" test has become the standard yardstick for determining subject matter jurisdiction in international securities fraud cases. Under the "conduct test," a federal court has subject matter jurisdiction if the defendant's conduct in the United States was more than "merely preparatory" to the fraud, and particular acts or culpable failures to act within the United States directly caused losses to foreign investors abroad. *Psimenos v. E.F. Hutton & Co.*, 722 F.2d 1041, 1045 (2d Cir. 1983); *IIT v. Vencap, Ltd.*, 519 F.2d 1001 (2d Cir. 1975). Under the "effects test," a federal court has subject matter jurisdiction where allegedly illegal activity abroad causes a "substantial effect" within the United States. *Consolidated Gold Fields PLC v. Minorco, S.A.*, 871 F.2d 252, 261-62 (2d Cir.), *cert. dismissed*, 492 U.S. 939 (1989). If either test is satisfied, subject matter jurisdiction exists. *See*

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[14] Respondents' amended complaint, in a single paragraph, alleges almost 35 different predicate acts of mail and wire fraud. (A-157-59 ¶ 107.)

[15] Satisfied with the substantial U.S. conduct it determined was sufficient to support jurisdiction (mail, wire and securities fraud), the Second Circuit did not belabor the point by cataloguing the additional U.S. conduct alleged by Respondents supporting jurisdiction (*i.e.*, the transportation of persons and money and securities worth more than $5000 in interstate or foreign commerce).

also Tamari v. Bache & Co., S.A.L., 730 F.2d 1103 (7th Cir.), *cert. denied*, 469 U.S. 871 (1984); *Grunenthal GmbH v. Hotz*, 712 F.2d 421 (9th Cir. 1983); *Continental Grain (Australia) Pty., Ltd. v. Pacific Oilseeds, Inc.*, 592 F.2d 409 (8th Cir. 1979); *Securities & Exchange Comm'n v. Kasser*, 548 F.2d 109 (3d Cir.), *cert. denied*, 431 U.S. 938 (1977).

2. **The Facts**

Both of the lower courts were dealing with essentially undisputed facts.[16] The record provides overwhelming evidentiary support for the following:

- *1983-to filing of complaint.* The participants in the fraudulent transactions were all United States citizens or businesses that operated in the United States and are thus subject to personal jurisdiction here. (E-1-6; E-22-24; E-150; E-185; E-282-83; E-317-18; E-378-79; E-392; E-394; E-396.)

- *September-December 1983.* The offering prospectus was conceived and drafted through the galley proof stage in the United States. (E-32-37; E-40; E-42; E-58; E-368-72; E-375-77.)

- *January 1984.* The express and stated aim of the offering was to raise funds for investment in the United States. (E-48; E-52.)

- *April 1984.* Before advancing subscription funds to SEIC, plaintiffs Abbar, Zainy and the Kanoos reviewed the Prospectus and relied upon its terms, including the promise that no more than 600,000 shares would be sold. (E-47; E-57; E-425; E-429; E-433.)

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[16] Petitioners list as one of the district court's factual findings the following: "Petitioners' actions in the United States were at most 'subsidiary' to the fraud alleged by respondents." (Pet. at 6.) Petitioners then proceed to state that "[t]he court of appeals did not disturb a single factual finding made by the district court." (Pet. at 8.) Obviously if the first statement is really a finding of fact, the second statement is nonsense, since the Second Circuit's entire decision rested on its conclusion that Petitioners' actions in the United States were substantially more than "subsidiary" to the fraud. In reality, the characterization of Petitioners' U.S. conduct as "subsidiary," "peripheral" or "substantial" is a legal, not a factual conclusion, and formed part of the Second Circuit's analysis.

- *April-June 1984.* Millions in investors' subscription deposits were placed in an "escrow deposit account" at European American Bank in New York prior to the closing. (E-45; E-67; E-71-72; E-102-04.) Other United States bank accounts were used as repositories for investors' deposits. (E-126; E-466-68.)
- *May-June 1984.* Sales of SEIC stock were made within the United States, causing a dilution of plaintiffs' shareholdings. (E-71; E-74; E-102-03; E-123; E-132-34; E-177; E-183-84; E-208-09; E-223; E-225-26; E-297-98; E-304; E-313-15; E-437-68.)
- *October 1984.* The offering closed in the United States. (E-67; E-71-72; E-119; E-120-21; E-126.)
- *October 1984.* The final stock certificates originated in and were exported from the United States, along with other documents containing misrepresentations and omissions which were transported to plaintiffs. (E-120, ¶ 3; E-142; E-148-52; E-198-99; E-202-07; E-210-19.)
- *October-November 1984.* Defendants do not deny, and there is evidence indicating, that substantial amounts of the Offering proceeds were converted in New York and diverted to investments in the United States for the benefit of Radwan, Fenn and a limited group of SEIC shareholders. (E-146 pt. 5; E-201.)
- *September 1984-October 1987.* Attempts were made to cover up the dilution in the United States. (E-142; E-164-66; E-177; E-183-84; E-208-09; E-223-25; E-273; E-297-310; E-313-15.)

Petitioners dispute very little of this. There is no question that Petitioners are United States citizens or were banks licensed to operate in the United States, and there is very little question about the events leading up to Respondents' receipt of the Prospectus.[17]

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[17] Petitioners and the district court take the position that the Prospectus, having gone to final print in Paris and having been disseminated in Europe, "cannot be said to have emanated from" the United States. (19a.) Respondents disagree, pointing to the fact that it was drafted, negotiated, and printed through the "galley proof" stage in the United States. The dispute generates more heat than relevance, however, since the venue of the Prospectus' printing has no bearing on the later activity that consummated the fraud and caused Respondents' losses.

Nor is there serious dispute about the activities that took place in the United States between April and June of 1984: no one denies that Reilly and the others negotiated and sold 180,000 shares of SEIC voting stock to Charles Keating's company ACC in Phoenix,[18] and 150,000 shares to Al-Turki in Houston.[19] Nor is there any dispute that the meetings, letters, telexes and telephone calls before and after those sales occurred when and where plaintiffs allege they occurred.[20] The only disagreement is over the legal relevance of those sales.

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[18] Although the 180,000 shares were ultimately held in the name of Lincoln American Investment Company N.V., an ACC offshore affiliate formed solely for that purpose, there is no question that ACC, an American company, was the beneficial owner. An internal SE Bank memorandum captioned "*American Continental's Investment in SEIC*" states:

> Today we received a call from ACC to inform us that you will be receiving a confirmation request from ACC's auditors concerning *the investment by ACC in SEIC stock*. The confirmation will be for a company called Phoenician Funding Corp (PFC), NV; this is a name change. The *investment arm* was formerly called Lincoln American Investment Corp.

(E-246) (emphasis supplied). In 1986, ACC obtained actual possession of its SEIC bearer share certificates and held them in the U.S. (E-293-95.) ACC's own records reflect that the SEIC stock was always recorded on the books of ACC as being an asset of an ACC domestic subsidiary. (E-312; E-313-15.) As for the entity Petitioners claim was the real owner of the 180,000 shares, Lincoln American Investment Company N.V. ("LAIC"), the admitted "investment arm" of ACC, all of the managing directors of LAIC were residents of Arizona and officers or employees of ACC. (E-858-59.) Even on Petitioners' own mailing list, the address for LAIC was Phoenix, Arizona. (E-133; E-243.) As the Second Circuit observed, the fact that a Netherlands Antilles "shell company" was created to be the "nominal purchaser does not detract from the import of the United States meetings and negotiations which preceded the sale." (8a-9a.)

[19] Petitioners make the staggering assertion that "the record is uncontradicted that SEIC did not oversell its offering of 600,000 shares. . . ." (Pet. at 9 n.10.) This is simply not true. The combined sales of 330,000 voting shares to ACC and Al-Turki prior to the Offering's closing in October clearly and unequivocally diluted all shareholders' interests. Reilly twice referred to the Offering as "oversubscribed" (E-120; E-124-25), and Fenn and Radwan sought to appease Keating for what they candidly referred to as the "dilution aspect." (E-208; E-224-26.)

[20] In order to demonstrate the alleged paucity of predicate acts supporting the Second Circuit's decision, Petitioners identify one telephone call, four telexes and

(Footnote continued)

Rather than acknowledge this as the determinative point of disagreement, Petitioners ignore the Second Circuit's conclusions and, like a mantra, repeatedly characterize all of the post-April conduct as "peripheral" or "incidental" or "subsidiary." Wishful thinking does not make it so. Petitioners' attempt at rhetorical sleight-of-hand permeates the entire petition and distorts both their rendition of the facts and their argument.[21]

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one letter as the only predicate acts purportedly relied on by the court to sustain jurisdiction. (Pet. at 9 n.11.) In fact, the record reflects many more instances of Petitioners' use of the mails and wires in furtherance of their scheme. *See, e.g.*, A-157 ¶ 107 (over 30 different predicate acts of mail and wire fraud). More significantly, Petitioners misconceive what the court did. In assessing jurisdiction under either the securities laws or RICO, the point of the exercise is not simply to identify and tally every single instance of mail and wire use. Rather, under the "conduct" test, the court must examine *all* conduct within the United States, which includes but is not limited to use of the mails and wire facilities. Such conduct here includes face to face meetings held between Petitioners and Charles Keating in Washington, New York, Arizona and Florida. (E-66; E-74; E-96; E-208; E-224-26; E-297-98; E-340-66.) Such conduct also includes the transportation in interstate and foreign commerce and the deposit of Offering proceeds in U.S. escrow accounts (A-140 ¶ 60; A-153-54 ¶¶ 97-99) and the diversion of those proceeds to purchase U.S. assets such as GOTCO. In short, for the purpose of establishing jurisdiction and a pattern under RICO, it is sufficient that there be at least two uses of the mail or wires in the context of other substantial U.S. activity. That standard is clearly met here.

[21] Petitioners' only direct response to the heart of the Second Circuit's analysis is buried in a footnote, which belittles but does not address the crux of this case:

> The court of appeals sought to bolster its reliance on wire and mail usage in the United States by reference to allegations that petitioners 'completed' the alleged fraud by diluting respondents' SEIC shareholdings through the Al-Turki and Lincoln N.V. sales. (8a.) This is curious, since any fraud upon respondents would have been complete as soon as respondents paid for their shares. . . .

(Pet. at 9 n.10.) Here, as throughout their brief, Petitioners present as unquestioned fact their version of the precise issue on which the courts below differed (*i.e.*, when the fraud was completed and the relevance of the substantial subsequent activity in the U.S.). The court of appeals did not "rely" on "allegations" that the fraud was completed by the dilution. The court analyzed the nature of the fraud alleged, the nature and scope of the conduct conceded, and the substantial body of existing law. Having done so, the court properly rejected what the petitioners propound as unchallenged cosmic law: that the fraud upon respondents was complete "as soon as respondents paid for their shares." *Compare* 6a-9a *with* Pet. at 9 n.10.

3. The Second Circuit's Application Of The Test To The Facts

a. Securities Fraud As The Racketeering Activity

The Second Circuit correctly held that the alleged fraud was not complete upon Respondents' receipt of the Prospectus. Respondents' amended complaint alleged violation of subsections (a), (b) and (c) of Rule 10b-5. (A-162 ¶ 120.) By so pleading, Respondents manifestly defined the fraud to include activities beyond the initial misrepresentations. Respondents' fraud theory is holistic, in the sense that it embraces a continuum extending from the Fall of 1983 (when the Prospectus was conceived and the galley proofs drafted in the U.S.), running through the Fall of 1984 (when bearer shares were finally issued and proceeds diverted for the personal benefit of Petitioners and certain favored shareholders) and extending until at least as late as 1986-87 (when Charles Keating and other ACC representatives conspired with Petitioners to conceal the fraud from Respondents and other shareholders).

Petitioners' fundamental error is in characterizing the alleged fraud as a mere purchase of stock in reliance on misrepresentations, and identifying the point of injury as the date Respondents deposited their subscription funds in escrow. This case is not the typical fraud case under Rule 10b-5(b), where the injury is complete upon the purchase of the stock because the facts represented are false *as of that time*. In this case, when Respondents transferred funds to pay for their SEIC stock, the fraud was still inchoate: Respondents' voting power remained undiluted and the proceeds had not yet been diverted. The acts that *directly caused* their injury — the oversubscribed sales to ACC and Al-Turki and the diversion of the stock proceeds — occurred later, in the United States.

The result reached here under the Second Circuit's exacting standard is consistent with that court's previous decisions.[22] In *IIT v. Vencap, Ltd.*, 519 F.2d 1001 (2d Cir. 1975), a Luxembourg

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[22] The Second Circuit's interpretation of the "conduct or effects" test has been described as the "most restrictive standard" in the country. *Zoelsch v. Arthur Anderson & Co.*, 824 F.2d 27, 30 (D.C. Cir. 1987).

investment trust and its three Luxembourg liquidators brought suit under the securities laws against a Bahamian venture capital firm. In addition to misrepresentations in and surrounding the agreement, plaintiffs also alleged post-agreement conduct in the U.S. that amounted to the funnelling of Vencap's funds into the hands of one of its officers. The Second Circuit held that the "subsequent acts" of funnelling Vencap's funds for personal benefit were the acts that "consummated the fraud" and, therefore, formed the basis for jurisdiction. Those acts are precisely analogous to the acts alleged here relating both to the dilution of Respondents' SEIC stock and Petitioners' ensuing diversion of funds.

The result below is also correct in light of *Psimenos v. E.F. Hutton & Co.*, 722 F.2d 1041 (2d Cir. 1983), a case in which there was far less U.S. activity than that which took place here. In *Psimenos*, the court held that it had jurisdiction over the Greek plaintiff's claims of fraud in the overseas purchases of securities, because Hutton's trades executed on American markets constituted "the culminating acts of the fraudulent scheme . . . ." *Id.* at 1044. Other circuits have also based jurisdiction on conduct that necessarily consummated the fraud. *See, e.g., Tamari, Grunenthal, Continental Grain*, and *Kasser, supra* at 21.

Thus, the Second Circuit's exercise of RICO jurisdiction here was correct: the court identified the alleged securities violations as racketeering activity; it analyzed the securities violations under the "conduct or effects" test and concluded that the "conduct" test had been met, citing substantial activity occurring in the U.S.; it identified numerous predicate acts of mail and wire use as part of the U.S. conduct. This is more than sufficient to sustain RICO jurisdiction over Respondents' claims.

b. Other Racketeering Activity

The predicate acts of securities fraud relied on by the Second Circuit were not the only racketeering activities alleged by Respondents. These other predicate acts also support jurisdiction under RICO.

Respondents have established numerous instances of wire and mail fraud in the U.S. which, when combined with Petitioners' other

illicit acts, constitute a pattern of racketeering activity.[23] Respondents also alleged that Petitioners engaged in a pattern of racketeering activity that included the transportation in interstate or foreign commerce of securities or money converted or taken by fraud, and in the execution and concealment of a scheme to defraud in violation of 18 U.S.C. § 2314. (*See, e.g.*, A-156 ¶ 104.) Finally, Respondents alleged Petitioners' furtherance of the scheme to defraud by mail and wire fraud in violation of 18 U.S.C. §§ 1341, 1343. (*Id.*)

In *Republic of the Philipines v. Marcos*, 862 F.2d 1355, 1358 (9th Cir. 1988) (*en banc*), *cert. denied*, 490 U.S. 1035 (1989), the Ninth Circuit upheld RICO jurisdiction where the underlying racketeering activity consisted of mail fraud, wire fraud and the transportation of stolen property. Although virtually all of the alleged underlying fraud took place overseas, the court of appeals sustained jurisdiction under the "conduct" test on the strength of the following U.S. activity: investment in California real estate of $4 million dollars of fraudulently obtained funds; creation of two U.S. bank accounts to hold $800,000 that had been fraudulently obtained; and transportation into Hawaii of money, jewels and other property, worth over $7 million, also fraudulently obtained.

Petitioners argue that the Second Circuit's decision in this case "squarely conflicts with" the *Marcos* decision. (Pet. at 3.) This statement is inexplicable. The conduct and predicate acts established by Respondents here far exceed those held sufficient in *Marcos* and clearly support the exercise of jurisdiction.[24] Indeed, since those acts occurred primarily in the United States, the lower court was not called upon to apply RICO "extraterritorially." There is ample justification for sustaining jurisdiction over Respondents' RICO claims on the basis of any or all of these grounds.

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[23] Mailings and wire communications between the United States and a foreign country in furtherance of a fraudulent scheme are sufficient for jurisdiction over mail and wire fraud violations. *United States v. Goldberg*, 830 F.2d 459, 461-64 (3d Cir. 1987); *United States v. Gilboe*, 684 F.2d 235, 239 (2d Cir. 1982), *cert. denied*, 459 U.S. 1201 (1983) (wire fraud); *United States v. Steinberg*, 62 F.2d 77, 77-78 (2d Cir. 1932), *cert. denied*, 289 U.S. 729 (1933) (mail fraud).

[24] Even the district court in the instant case, whose decision Petitioners would reinstate and enshrine, believed RICO jurisdiction would exist if measured by the standard applied in *Marcos*. (23a.)

C. Jurisdiction Is Appropriate Under Section 403 Of The Restatement

Section 403 of the Restatement (Third) of Foreign Relations sets out eight factors to be considered in determining whether it is "reasonable" for a U.S. court to exercise subject matter jurisdiction over a transnational dispute. Sections 403(2)(a) and 403(2)(b) correspond most closely to the "conduct" test. As amply established above, the facts in this case satisfy the "conduct" test and, therefore, they also satisfy the first two criteria of Section 403.

The exercise of jurisdiction here is reasonable under the six remaining criteria as well. The citizenship, domicile, and residence of the central figures in this case, the locus of their fraudulent activity, and the acknowledged purpose of their undertakings, support the conclusion that the assertion of subject matter jurisdiction is reasonable under the circumstances presented here.[25]

D. The Second Circuit's Decision Is Neither Revolutionary, Dangerous, Nor Likely To Lead To Disastrous Results

Petitioners issue a shrill call to alarm, suggesting that the Second Circuit has created a revolutionary new rule. They predict that this new rule will throw open the floodgates, forcing U.S. courts to entertain RICO suits arising out of transactions negotiated in a "Turkish bazaar," so long as the transaction is "confirmed by two telephone calls to New York." (Pet. at 16.)

This is nonsense. From the start, Petitioners have attempted to paint this action with a xenophobic brush. First it was "[A]rabs chasing after [A]rabs" (A-87);[26] now it is "Persian rugs in a Turkish bazaar." (Pet. at 16.) Their view of Respondents' fraud action simply

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[25] Professor Andreas Lowenfeld, one of the reporters of the Restatement, submitted a compellingly reasoned and extensive affidavit to the district court. After extensive analysis, Professor Lowenfeld concluded that the exercise of subject matter jurisdiction over Respondents' securities fraud claims is reasonable under the Restatement. (E-469-98.) The same logic and analysis support jurisdiction under RICO as well.

[26] Indeed, one of the Petitioners' counsel jibed:

> We're talking about who's behind which sand dune, got off which camel and said what to whom [–] who then got on some other camel and rode off into the distance. That's what this case is about.

(A-248.)

ignores the overwhelming record evidence of substantial, substantive conduct within the United States by United States citizens, as well as the liberal use of the U.S. mails and wires to effectuate that conduct.

It also bears emphasis that the issue here is subject matter jurisdiction under RICO, an expansively interpreted statute. Both Congress and this Court have directed the lower courts to construe RICO liberally, in order to implement its remedial purposes. *Sedima, S.P.R.L. v. Imrex Co.*, 473 U.S. 479 (1985). Indeed, RICO has proven uniquely resistent to floodgate threats. Responding to similar arguments that civil RICO was sweeping unintended behavior into its maw, this Court has stated:

> The "extraordinary" uses to which civil RICO has been put appear to be primarily the result of the breadth of the predicate offenses, in particular the inclusion of wire, mail and securities fraud, and the failure of Congress and the courts to develop a meaningful concept of a "pattern."

Id. at 500. In any event, Respondents allege that funds illegally obtained through fraudulent misrepresentations made by U.S. citizens were transported to and invested in banks and businesses in this country. This is precisely the type of conduct RICO was intended to remedy in an era of rampant transnational chicanery.

In determining that jurisdiction exists in this case, the Second Circuit broke no new ground. It measured the allegations of conduct in this country by the yardstick of a standard so well-established it is enshrined in the Restatement. It applied that well-worn standard to a statute which is to be liberally construed to remedy a broad spectrum of offenses affecting interstate or foreign commerce. The undisputed facts betray the overwhelming and legally relevant conduct that took place in the United States. The long-existing law of the Second Circuit and other courts mandates the exercise of jurisdiction in light of those facts.

There is nothing controversial, radical or dangerous about the Second Circuit's decision. Its judgment was correct.

CONCLUSION

For all of the foregoing reasons, the petition for a writ of certiorari should be denied.

Dated: New York, New York
November 15, 1991

Respectfully submitted,

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(3)

No. 91-641

IN THE

Supreme Court of the United States

OCTOBER TERM, 1991

RICHARD A. FENN; JAMAL RADWAN; SAUDI EUROPEAN INVESTMENT CORPORATION N.V.; ALEF INVESTMENT CORPORATION N.V.; ALEF BANK, S.A.,

Petitioners,

—v.—

ABDULAZIZ A. ALFADDA; ABDULLAH ABBAR; ABDULLA KANOO; ABDULAZIZ KANOO; YUSIF BIN AHMED KANOO (a Partnership Company); AHMED A. ZAINY,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

REPLY BRIEF IN FURTHER SUPPORT OF PETITION

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

REPLY BRIEF IN FURTHER SUPPORT OF PETITION

Petitioners submit this reply brief in further support of their petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the Second Circuit in this case.

It is plain from the face of its opinion that the court of appeals did *not* apply to civil RICO the "substantial conduct or effects in the United States" test for determining United States subject matter jurisdiction. Rather, the Second Circuit ignored this test—adopted by every other federal court that

has addressed the issue and endorsed by the Restatement (Third) of the Foreign Relations Law of the United States (1987)—and instead crafted an entirely different standard that greatly expands the extraterritorial reach of civil RICO.

Respondents now attempt to avoid review of the Second Circuit's test for RICO subject matter jurisdiction by presenting a response rife with irrelevant factual issues. None of the new purported bases for jurisdiction argued by respondents in their opposing brief was accepted by the court of appeals or the district court, and none is supported by the evidence in the record.

ARGUMENT

THE COURT OF APPEALS REFUSED TO APPLY THE "CONDUCT OR EFFECTS" TEST IN ASSERTING JURISDICTION OVER RESPONDENTS' RICO CLAIM.

Respondents challenge petitioners' showing that the Second Circuit failed to apply to civil RICO the traditional test of "substantial conduct or effects in the United States" to determine whether a transnational transaction is to be governed by United States law. (Opp. Br. 17-19.)[1] The opinion of the court of appeals, which grounds subject matter jurisdiction over respondents' RICO claim entirely upon the alleged use of United States mails and wires a handful of times in connection with subsequent sales to two foreign nonparties, is clear. After identifying petitioners' alleged use of the mails and wires regarding those sales (5a-6a), the Second Circuit held:

> "The sales to Lincoln American Investments and Al-Turki were predicate acts which occurred primarily in

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1 References to "Opp. Br. _____" are to respondents' brief in opposition to this Petition. References to "_____ a" are to the pages of the Appendix to the Petition. References to "A _____" or "E _____" are to the pages of the Joint Appendix and Exhibits, respectively, filed in the court of appeals.

> the United States, *and hence, serve as a basis of subject matter jurisdiction for the RICO claims.*"

(11a) (emphasis added).

The court of appeals—which expressly acknowledged the applicability of the "substantial conduct or effects" test to respondents' federal securities law claim—did not once invoke that limitation upon the extraterritorial application of domestic statutes when it asserted jurisdiction over respondents' RICO claim. (9a-11a.) Far from requiring substantial conduct or effects in the United States to sustain the application of civil RICO to the foreign transactions at issue, the Second Circuit accepted respondents' argument that this test is not applicable in the civil RICO context.[2] The Second Circuit created an entirely different test for civil RICO subject matter jurisdiction, in which two predicate acts involving the wires or mails in the United States will suffice to make an otherwise wholly foreign transaction subject to United States substantive law.[3]

RESPONDENTS PRESENT AS "FACT" UNSUPPORTED ASSERTIONS WHICH NEITHER THE COURT OF APPEALS NOR THE DISTRICT COURT ACCEPTED.

Rather than defending what the Second Circuit actually decided, respondents now present this Court with unsupported theories of subject matter jurisdiction which

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2 Respondents maintained that "[t]here is no basis in law or logic to engraft the conduct and effects tests used in the securities fraud context onto RICO. The court below committed error in having done so. . . ." (Respondents' Brief on Appeal to the Second Circuit, dated February 8, 1991, at 46.)

3 The holding of the court of appeals has been so understood by the district court. *Bank of Crete, S.A. v. Koskotos*, No. 88 Civ. 8412 (KMW) (S.D.N.Y. Aug. 30, 1991), citing *Alfadda v. Fenn*, 935 F.2d 475, 479 (2d Cir. 1991).

were not accepted by the court of appeals or the district court.[4]

A. The District Court Expressly Found That The Representations Upon Which Respondents Allegedly Relied Were Made In The Middle East.

Respondents admit that they received the Private Placement Memorandum upon which they allege reliance in the Middle East. (Opp. Br. 8.) However, respondents now assert that the Private Placement Memorandum was "drafted and prepared in the United States." (Opp. Br. 6.) That is flatly incorrect: the district court expressly found that the Private Placement Memorandum "was prepared primarily outside the United States, and cannot be said to have emanated from here." (19a.) The court of appeals in no way disturbed that factual finding.

B. Respondents' Assertions Of Injury To SEIC Have No Relevance To Their Claim.

Respondents argue that petitioners' alleged fraud was not "consummated" until the alleged post-1984 diversion and misuse of the proceeds of the SEIC share offering. (Opp. Br. 11-12.) The district court properly rejected this claim, holding that any fraud on these respondents

> " 'was committed by placing the allegedly false and misleading prospectus in the purchasers' hands'. . . Here, it is uncontroverted that the prospectus was sent to the plaintiffs from Paris or Geneva, or hand-delivered in Saudi Arabia or Bahrain."

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4 Respondents do not challenge petitioners' showing that, in the face of an evidentiary attack, respondents had the burden of proof in establishing subject matter jurisdiction. *See Thornhill Publishing Co. v. General Tel. & Elec. Corp.*, 594 F.2d 730, 733 (9th Cir. 1979) (and cases cited therein); 13 C. Wright, A. Miller & E. Cooper, *Federal Practice & Procedure: Jurisdiction 2d* § 3522, at 63-65 (1984).

(18a) (citing *Bersch v. Drexel Firestone, Inc.*, 519 F.2d 974, 987 (2d Cir.), *cert. denied sub nom. Bersch v. Arthur Andersen & Co.*, 423 U.S. 1018 (1975)).[5]

Neither the court of appeals nor the district court has ever held that respondents' claim of diversion of the proceeds of the SEIC offering is at issue in this litigation. Since any claim that the offering proceeds were diverted from SEIC belongs to SEIC, and could only be asserted by or on behalf of SEIC, respondents lack standing to sue on such a claim.[6]

Respondents' allegations of lost corporate opportunities for SEIC are also claims belonging solely to SEIC.[7] The assertion that certain "favored shareholders" of SEIC participated in transactions at SEIC's expense (Opp. Br. 11-12) does not allege an injury specific to respondents, since such actions, even if true, would have equally affected the value of *all* shares of SEIC.[8] In sum, each of the asserted injuries to respondents is not an injury to respondents themselves, and thus has no place in this action.

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5 Subject matter jurisdiction would not exist even if the fraud alleged by respondents was incomplete until respondents paid for their SEIC shares and until SEIC issued additional shares which allegedly "diluted" respondents' SEIC shareholdings, because this conduct did not occur in the United States. Respondents paid for their shares abroad (E 496-97, 640-41, 697-729); respondents themselves allege that petitioners' authorization to issue additional SEIC shares occurred entirely abroad. (A 146-47.)

6 *See, e.g., Sears v. Likens*, 912 F.2d 889, 892 (7th Cir. 1990); *Adams-Lundy v. Association of Professional Flight Attendants*, 844 F.2d 245, 250 (5th Cir. 1988); *Roeder v. Alpha Indus., Inc.*, 814 F.2d 22, 29 (1st Cir. 1987); *Rand v. Anaconda-Ericsson, Inc.*, 794 F.2d 843, 849 (2d Cir.), *cert. denied*, 479 U.S. 987 (1986); *Warren v. Manufacturers Nat'l Bank*, 759 F.2d 542, 544 (6th Cir. 1985); *Stevens v. Lowder*, 643 F.2d 1078, 1080 (5th Cir. 1981).

7 *See Abrams v. Donati*, 66 N.Y.2d 951, 952, 489 N.E.2d 751, 752, 498 N.Y.S.2d 782, 783 (1985); 13 *Fletcher Cyclopedia of the Law of Private Corporations* § 5941.10 (1991).

8 The district court thus specifically noted that respondents' allegations regarding Gulf Oil Trading Company ("GOTCO") (Opp. Br. 11-12, 24) were purely derivative. (A 78.)

C. Respondents' Assertion Regarding The Planned Investment Of Offering Proceeds Has No Relevance To Their Claim.

Respondents urge the Court to approve the finding of subject matter jurisdiction over their RICO claim by virtue of SEIC's plan to invest a portion of the offering proceeds in the United States. (Opp. Br. 6-7.) There can be no fraud in that fact, however, since the Private Placement Memorandum expressly disclosed that this use was among the purposes of the SEIC offering. (A 178.)

Neither the court of appeals nor the district court accepted this argument when respondents presented it below. Respondents' argument would require United States courts to apply United States law to, for example, securities fraud claims by Japanese investors who purchased, in Japan, stock in a Japanese automobile manufacturer which thereafter planned to invest funds in the United States. That cannot be the law.

D. The Individuals, Entities and Actions Involved In Respondents' Stock Purchases Were Overwhelmingly Foreign.

The court of appeals did not disturb the district court's express finding that none of the respondents and only one of the petitioners was a United States resident. (24a-25a.) Despite this factual determination, respondents now go to great lengths to demonstrate that some of the petitioners conducted some business in the United States. (Opp. Br. 3-5.)[9]

That has never been in issue. The question faced by the courts below was not whether there is personal jurisdiction over petitioners, but rather whether there is subject matter

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9 Respondents' assertion that petitioner Jamal Radwan "spends much of his time in New York" (Opp. Br. 3) grossly misstates the record. Examination of the citation for that statement reveals that Radwan is president of a bank in Paris, has a home in England, and spends "most of the year" in Geneva, Paris and Bahrain in addition to business travel to New York. (E 392.) The district court expressly found that Radwan "appears from all the materials submitted to be a resident of France, not of the United States." (24a-25a.)

jurisdiction over respondents' claims. As the district court properly held, the focus in that inquiry is upon the extent of United States activities in connection with the overseas representations to, and share purchases by, these Saudi Arabian and Bahraini respondents. (22a-25a.)[10]

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10 Respondents' claim that the actions of Ronald Reilly and Mario Diaz-Cruz, III, somehow confer jurisdiction over their RICO claim is unsupported in the record. Reilly's work with SEIC began in Paris in mid-October 1983, where he negotiated his contract with SEIC. (E 734, 846-47.) During his preparation and marketing of the 1984 SEIC private placement, Reilly maintained his office in Paris. When he was not in Paris, he was travelling in Europe and the Middle East. (E 734, 739-61, 840-41, 849.)

There is no suggestion that Diaz-Cruz was in any way involved in representations to respondents in the Middle East in the first part of 1984, when respondents learned of the private placement and made their share purchases. While respondents harp on Diaz-Cruz's involvement in September and October 1984 in the printing of SEIC stock certificates and drafting of form letters and share custody certificates (Opp. Br. 10-11), these events occurred many months after respondents had paid for their shares. (E 148-52, 199, 203-07.) Moreover, the letters in question were neither sent to respondents from the United States nor were they sent by Diaz-Cruz. (E 210-15.)

CONCLUSION

For the foregoing reasons and the reasons set forth in petitioners' opening memorandum, the petition for a writ of certiorari should be granted.

Dated: New York, New York
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